FROM THE LEADERSHIP ARCHIVE

The Place for Ethics in Organizations

How can executives ensure that their companies' policies are fair and ethical? What steps can organizations take to make a positive impact on the world around them?

Contents

Introduction

Individual and organizational ethics can be tricky things, especially in an age of disruption, where the managerial mantra is “break the rules.” This collection of articles from *MIT Sloan Management Review* looks at some of the specific areas where ethics play a role in operations, including strategic decision-making, data collection, and sustainability performance.

From “The Trouble With Corporate Compliance Programs”:

- Many corporate leaders believe that rigorous compliance programs will prevent employee wrongdoing. And if something does go wrong, the hope is that having a comprehensive program will help convince regulators that the company’s compliance and ethics initiatives were “effective.”
- But to really prevent employee wrongdoing, companies need to understand how employees reach unethical decisions and what affects their decision-making processes.
- Behavioral ethics research finds that people default toward acting unethically because they are driven by self-interest, and that they find ways to convince themselves — consciously and subconsciously — that they are acting ethically.
- While no program will entirely change our cognitive processes or stop all unethical behavior, there are three cost-effective steps companies can take to combat rationalizations.

From “Which Rules Are Worth Breaking?”:

- Disruption of an established business model requires companies to think creatively and disregard the status quo and break the existing rules of the game.
- But there’s risk in defying too many rules.
- Uber, for example, clearly became successful by approaching the ride-hailing market in all new ways, but in 2017 it also become a poster child for bad behavior.

- Disruptive companies like Uber need to move away from the perspective that rules and norms don't matter and embrace a more specific understanding of *which* rules are worth breaking and why.

From "Ethics Should Precede Action in Machine Intelligence":

- U.S. Census Bureau chief scientist John Abowd warns that it's growing increasingly difficult to protect personal data in a world where people are getting better and better at re-identifying "anonymized" entries. "What was implausible in the twentieth century is now plausible," he says.
- In their book *The Mathematical Corporation*, Josh Sullivan and Angela Zutavern write that ethical conflicts continue to arise as the ability of companies to collect and parse personal data explodes.
- They pose this question: "If we agree that lying, deceiving, stealing, and harming are unethical, which situations in your business become question marks?" For instance, they write, a media lab in the Netherlands assembled a database of Dutch citizens' birth dates, professions, addresses, sexual orientations, and even medical histories using only publicly available data. "How personal, private, and usable are these data? Can you ethically use it? We think not," they conclude.
- "Presuming you follow the law, you still have to clarify your ethical philosophies and those on which your organization stands," they write.

From "Why the Business Case for Sustainability Will Win Out":

- The Trump administration's 2017 dismissal of U.S. climate promises casts a shadow over climate change commitments by the country.
- U.S. corporations still have incentives to move forward on their own climate reduction plans, which have been built on solid business cases.
- "Fossil fuels contribute directly to climate change," wrote Anheuser-Busch chief sustainability and procurement officer Tony Milikin in a column published the same day as Trump's declaration that he would withdraw the United States from the 2016 Paris climate agreement. "By initiating long-term agreements with clean-energy providers, businesses can provide stable demand and the capital for further investment in local renewable energy infrastructure projects," Milikin wrote.

Buying renewable energy makes good business sense, too, he added: “In some markets, renewable energy purchased via PPAs [power purchase agreements] is cheaper than grid-sourced electricity.”

- Anheuser-Busch is not an outlier. More than 1,200 U.S. governors, mayors, and businesses signed an open letter pledging that “We Are Still In,” with Apple, Campbell Soup, General Electric, Facebook, Tesla, and Walmart all saying that they are continuing with company-specific plans to battle climate change.

From “Corporate Sustainability at a Crossroads”:

- *MIT Sloan Management Review* and The Boston Consulting Group tracked corporate sustainability programs from 2009 to 2016.
- The cumulative findings show that while corporate leaders in sustainability remain a minority and are unevenly distributed across geographies and industries, a handful of standout companies are demonstrating that sustainability can be a driver of innovation, efficiency, and lasting business value.
- We identified eight evidence-based factors that drive sustainable business practices.
- For instance, Key Lesson Seven is to develop a compelling sustainability value-creation story for investors. Only 60% of corporate executives think investors care about sustainability performance, but in fact 75% of executives in investment companies think sustainability performance should be considered in investment decisions.

From “Ethics and the Algorithm”:

- Advances in information technology have made the use of data — principally data about our own behaviors — ubiquitous in the online experience.
- Companies tailor their offerings based on the technology we employ — for example, news stories are suggested based on our previous reading habits. Yahoo, Facebook, and Google tailor the order, display, and ease of choices to influence us to spend more time on their platforms, so they can collect even more data and further intermediate our daily transactions.
- But the software code used to make judgments about us based on our preferences is not value-neutral — it contains conclusions about who we are and how we

should live. Should we have access to many choices? Should we be subtly influenced to buy from a particular online vendor?

- We need to figure out how to have better conversations about the role of purpose, ethics, and values in this technological world, rather than simply assuming that these issues have been solved.

From “Combining Purpose With Profits”:

- If you want to build a company that truly motivates its employees, it has to have a sense of purpose.
- To sustain both a sense of purpose and a solid level of profitability over time, companies need to pay attention to several fundamental organizing principles, including the need for support systems that reinforce goals.
- This article includes three mini cases: Sweden’s Svenska Handelsbanken, India’s Tata Group, and India’s HCL Technologies.
- This article was awarded the 2015 Richard Beckhard Memorial Prize for outstanding *MIT SMR* article on planned change and organizational development.

The Trouble With Corporate Compliance Programs

Companies with rigorous compliance programs hope such programs will curtail employee wrongdoing. But to prevent employee misconduct, companies also have to understand how employees reach unethical decisions — and what affects their decision-making processes.

Todd Haugh

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Multinational corporations spend millions of dollars per year on compliance. In highly regulated industries such as health care and finance, large companies spend much more, sometimes hiring hundreds or even thousands of compliance officers at a time.[1] Siemens AG reportedly spent more than $1 billion on an internal investigation related to a government inquiry into the company's payment of foreign bribes.[2] But the costs are not just financial. Compliance programs are aimed at eliminating the time-consuming and distracting regulatory and legal processes that accompany ethical failures.

There is a belief on the part of corporate leaders that when rigorous compliance programs are in place, employee wrongdoing will largely disappear. If something does go wrong, the hope is that having a comprehensive program will help convince regulators that the company's compliance and ethics initiatives were "effective" (the standard set by U.S sentencing guidelines).[3]

Companies strive to make their programs as "bulletproof" as possible. Unfortunately, even the most comprehensive programs won't curtail corporate wrongdoing or the government intervention that follows. For instance, Volkswagen AG's compliance program didn't stop employees from installing "defeat device" software to cheat emissions tests, nor did Wells Fargo & Co.'s policies prevent its employees from opening new customer accounts without customers' authorization. More than 15 years after the Enron scandal, most companies know very little about how employees make ethical decisions or the psychological mechanisms that cause them to perform unethical and illegal acts. Even fewer companies have compliance strategies aimed at curbing such behaviors.

The goal of this article is to pull together the burgeoning field of behavioral ethics, which provides insight into how individuals make ethical decisions, with the work of criminologists who study individual and corporate criminality. My aim is to help business leaders see why their corporate compliance efforts are falling short and how those efforts can be improved. In addition, I will offer some practical and cost-effective steps for improving compliance programs that focus on employee behavior — the best way to make compliance truly effective.

Dual Systems of Thinking

Corporate compliance depends on the behavior of individual employees. If employees, officers, and managers always acted in a law-abiding and ethical manner, compliance failures would rarely occur. Of course, that is not realistic. That is

why companies need to be aware of how and why employees act the way they do. This starts with understanding how people make decisions generally and how that translates into ethical decision-making.

Contrary to traditional economic theory, people don't make strictly rational decisions. Instead, as the work of psychologists Daniel Kahneman and Amos Tversky revealed, most decisions are influenced by dual cognitive processes: intuitive and reasoning.[4] The intuitive process (which Kahneman and Tversky refer to as System 1) is "fast, automatic, effortless, associative, and often emotionally charged."[5] It operates by associative memory and habit, which makes it difficult to control or modify. A lot happens at once through System 1 — the mind offers associations rapidly, one idea after another, all linked effortlessly. The speed and ease by which System 1 operates means that "most of the work of associative thinking is silent, hidden from our conscious selves."[6]

The reasoning process (referred to as System 2) is more serial and deliberate. It is engaged when we use thought in an organized manner. We use it to solve complex math problems, write a paragraph, or contemplate multifaceted decisions when there aren't easy associations to make. System 2 thinking gives us the "experience of agency, autonomy, and volition."[7] Not surprisingly, the reasoning process requires much more mental effort than using intuition. Reasoning isn't necessarily better than intuitive thinking — you wouldn't want to reason your way through every one of your day-to-day tasks — but for the most important decisions, it's critical. Yet, because System 2 thinking takes

more effort, our minds have developed to rely primarily on System 1, reserving System 2 either for the most challenging mental tasks or to correct errors in our automatic thinking. This may seem fine, but research shows that people often use System 2 to justify their System 1 conclusions.[8] Instead of correcting errors, sometimes our reasoning process reinforces our often flawed intuitions.

Although Kahneman and Tversky did not study ethical decision-making directly, their findings are critical to understanding how people make decisions in an ethical context. Behavioral ethics researchers have taken the insights of dual system thinking and applied them to ethical decision-making in business. They have found that while most people intend to act ethically, good people often do bad things.[9] Indeed, research has found that self-interest is associated with intuitive thinking.[10] Despite this, most of us act ethically most of the time. That is because System 2 is properly functioning as an ethical monitor, jumping in to control the automatic self-interest each of us possesses.[11]

Rationalizing Unethical Behavior

If System 2 is an ethical monitor, why does it seem to fail so often? For example, what enabled VW employees to install the code used to defeat emissions tests? Although behavioral ethics research helps us understand how the brain works, it doesn't explain what allows the brain to take that critical step toward unethical behavior.

This is where criminology, the study of crime and criminals, comes in. Criminologists

researching white-collar crime have theorized that three conditions are necessary for a corporate crime to occur.[12] First, an individual must possess a problem he or she feels cannot be solved by revealing it to others. A "non-shareable problem" might be anything from gambling debts to the prospect of job loss — anything that the person is deeply concerned about. Second, the individual must believe that the problem can be solved in secret by violating a trust. As corporate leaders know, trust is an essential element in any organization — almost every principal-agent relationship is built upon it. Third, the individual must have an internal dialogue about the problem and the unethical — even illegal — solution that makes the trust violation seem acceptable.[13] The classic example is the banker who tells himself he is only "borrowing" the embezzled funds and will pay them back later.

The last step, which criminologists call "verbalizations" (and the rest of us usually refer to as rationalizations or even excuses), is the crux of white-collar crime. Criminologists don't view verbalizations as simple, after-the-fact excuses that offenders use to relieve their culpability upon being caught. Instead, they see them as "vocabularies of motive" — words and phrases offenders use to make bad behavior seem appropriate.[14] This means that an offender's rationalizations are created before acting and actually allow the bad act to proceed. As the criminologist who developed rationalization theory puts it, "[t]he rationalization is [the offender's] motivation."[15] Rationalizations, which have been identified in numerous studies, permit white-collar offenders

to act in ways that they would otherwise deem unacceptable.

This is consistent with what we know about how people make unethical decisions. Behavioral ethics research does not suggest that everyone wants to act ethically but fails to do so because of cognitive obstacles. Rather, people default toward acting unethically because they are driven by self-interest, and then they find ways to convince themselves — consciously and subconsciously — that they are acting ethically.[16] This appears to be a case of System 2 justifying System 1 conclusions. It's likely this process is a product of our unique evolution. Although the ability to cooperate with one another is one of humankind's greatest advantages, the best course of action from an individual perspective is often to act in one's self-interest.[17] Thus we have developed mechanisms to deal with the countervailing aspects of living in our "hypersocial" yet competitive world.[18] One of the mechanisms is to rationalize our behavior — to reframe how we look at it in order to align our self-perception as a "good person" with the unethical or illegal behavior we are contemplating. There is no better way to act self-interestedly while simultaneously projecting to others (and ourselves) that we are good members of a cooperative society.

I believe that rationalization theory, which has greatly influenced the study of both white-collar crime and business ethics, explains what happens when an individual's ethical monitor is overcome.[19] Essentially, rationalizations trick the System 2 reflective thinking process that normally intervenes to contain our unethicality.

Once this happens, there is nothing to stop a person from committing an unethical or illegal act, regardless of the organizational norms, business regulations, or criminal laws in place.

ABOUT THE RESEARCH

This article is part of my long-term study of the causes of white-collar crime and corporate wrongdoing. After approximately a decade representing white-collar defendants in state and federal court, advising companies on corporate compliance practices, and drafting guidelines to aid federal judges in sentencing fraud offenders, I found that the standard narratives of why businesspeople commit bad acts were misguided. This led me to criminological theory and sociologist Donald Cressey's groundbreaking study of embezzlers, which revealed the role rationalizations play in violations of organizational trust. Using Cressey's research as a point of departure, I have undertaken projects analyzing sentencing disparities among economic crime defendants, professional athletes who committed and were victim to fraud, defendants convicted of the theft of cultural heritage resources, and numerous individual and corporate case studies focused on the behavioral aspects of white-collar and organizational crime. Collectively, this research has helped me identify prominent rationalizations used by white-collar offenders and confirmed the importance of behavioral insights for effective corporate compliance, white-collar sentencing, and criminal legislation.

What are the most typical rationalizations? And more importantly, how do we identify them? My research suggests there are eight

rationalizations most commonly used by those committing unethical and illegal acts within companies.[20] (See "About the Research.") As part of an effective compliance program, corporate leaders need to understand these rationalizations and be able to identify their usage.

Denying Responsibility

Offenders use this rationalization to relieve themselves of responsibility, thereby mitigating social disapproval and a personal sense of failure. White-collar offenders deny responsibility by pleading ignorance, suggesting they were acting under orders, or contending that larger economic conditions caused them to act illegally. This may be considered the catchall rationalization leading to wrongful conduct.

Denying Injury

This rationalization focuses on the injury or harm caused by the illegal or unethical act. If an act's wrongfulness is a function of the harm it causes, an offender often excuses his or her behavior if no clear harm exists. Offenders employ this rationalization when the victim is insured or the harm is to the public or market as a whole, such as in insider trading or antitrust cases.

Denying the Victim

Denying the victim takes two forms: when the offender argues that the victim's actions were inappropriate and therefore the victim deserved the harm; or when the victim is unknown or not clearly defined. White-collar offenders often use

this rationalization when committing frauds against the government, such as in false claims or tax evasion cases.

Condemning the Condemners

This rationalization shifts attention away from the offender’s conduct to the motives of others, such as regulators, prosecutors, and government agencies. It can take various forms: The offender calls his or her critics hypocrites, argues that they are compelled by personal spite, asserts they are motivated by political gain, or complains about selective enforcement.

Appealing to Higher Loyalties

Individuals use this rationalization when they are willing to sacrifice societal norms to advance the interests of a group to which they belong. The actions are needed, the offender argues, to protect a boss or employee, shore up a failing business, or maximize shareholder value. For example, if an employee argues that he or she committed a fraud not for personal gain but to help the company, he is or she is likely using this rationalization.

Using a Ledger Metaphor

This rationalization is based on a “behavioral balance sheet” whereby people balance their negative actions against their positive accomplishments, thus minimizing their sense of moral guilt. Senior executives, particularly those active in philanthropy, are especially prone to this type of rationalization.

Claiming Entitlement

People involved in employee theft and embezzlement cases frequently use this rationalization in the belief that they deserve the fruits of their illegal behavior. This rationalization is also common in public corruption cases.

Claiming Relative Acceptability or Normality

This rationalization compares the offender's bad acts with those of others to relieve moral guilt. Tax violators and those involved in real estate, accounting, and trading fraud often rationalize their actions by citing the behavior of others. It may be particularly prevalent when a negative organizational culture is strong and insulated.

How Rationalizations Undermine Compliance Programs

There are plenty of practical examples illustrating how employees rationalize behavior that leads to compliance issues. The experiences of Intel Corp. and Wells Fargo are instructive.

In the early 2000s, Intel adopted an aggressive approach to compliance in order to curb potential antitrust violations by its sales executives.[21] It devised a program in which the company's compliance professionals periodically conducted random audits in which they searched through papers, emails, and other electronic records of managers, seizing anything that might be sought as part of a government investigation. If the company found irregularities, it sometimes even held mock depositions of the offending executives, using outside antitrust lawyers. Intel's general counsel explained that these role-playing exercises served as a wake-up call, giving lax

executives the experience of being in the government's crosshairs. He boasted that Intel's aggressive approach to compliance was "the world's best."[22]

Yet Intel was unable to avoid government intervention in its business. Intel spent years in private antitrust litigation, and in 2009 the New York attorney general sued the company, arguing its compliance program not only was ineffective but had helped contribute to illegal anticompetitive behavior by appearing to have communicated to employees that the goal of the compliance initiatives was to limit mention of illegal behavior, rather than to eliminate the behavior.[23] Based on my analysis of employee emails revealed as part of the lawsuit, the company's approach may have facilitated a host of rationalizations, including two mentioned above: denial of injury and denial of the victim. In addition, employees more easily denied their responsibility, the catchall rationalization, because anticompetitive practices were seen as part of doing business at Intel.

Wells Fargo's recent difficulties appear to offer another example of rationalized corporate wrongdoing. The company's fake-account scandal demonstrates how executives can affect the context in which employees make decisions regarding ethics. Details of how exactly the bank's ethics and compliance program operated are still emerging, but preliminary reports suggest it allowed an environment riddled by employee rationalizations. On the heels of the bank's $185 million settlement agreement with the Consumer Financial Protection Bureau, a number of former employees have reported that despite ethics training and messages from

headquarters to not create fake accounts, the bank's aggressive sales culture drowned out any explicit compliance measures. Essentially, the compliance program failed to address the systemic problem of managers pressuring employees to meet unrealistic sales goals.[24] "The reality was that people had to meet their [sales] goals," one former employee explained. "They needed a paycheck."[25] This suggests that employees, under pressure to meet unrealistic goals, rationalized their conduct by denying responsibility and claiming relative normality.

Combating Rationalizations

Behavioral science, coupled with criminological insights, indicates there are complex, interwoven, and deeply seated psychological processes at work that can undermine even the best compliance program. So what are companies to do? Is there a way to do compliance better — one that solves some of the problems created by the automaticity of self-interest we all possess? Yes, but it requires a fundamental shift in corporate thinking.

The best approaches to compliance focus not on how government regulators will react to a compliance initiative but on how employees — the real "customers" of compliance — will be affected. They consider the behavioral implications of the compliance program at every turn, particularly how company policies might foster or defeat employee rationalizations. While no program will entirely change our cognitive processes or stop all unethical behavior, there are three cost-effective steps companies can take.

Hire a behavioral specialist. Although dual-system thinking, rationalization, and behavioral ethics theories have been around for decades, their application to business and compliance is still in its infancy. Hiring a behavioral specialist or developing someone internally to stay abreast of the various fields and their increasing insights into ethical decision-making is a good first step.

One of the tasks a behavioral specialist can take on is to educate the organization, particularly the compliance team and HR staff, on key takeaways from current research in the fields of behavioral ethics, behavioral economics, moral psychology, and criminology.[26] Books on decision-making and dishonesty by serious researchers, yet aimed at more general readers, can be a helpful resource.[27] A company's behavioral specialist should create a behavioral compliance curriculum tailored to various groups of employees, giving all members of the organization insight into their ethical decision-making processes. Such a curriculum can become the backbone of a behaviorally cognizant compliance program.

Use behavioral best practices to eliminate rationalizations. To create compliance programs that take advantage of behavioral insights instead of falling prey to them, companies must start to adopt compliance practices driven by the behavioral science at the heart of criminology and behavioral ethics. This will necessarily go beyond the traditional law-driven compliance practices employed by the vast majority of Fortune 500 companies.

If rationalizations are the crux of employee wrongdoing, then compliance programs should be aimed at eliminating them. One possibility is to ask employees to sign a certification before they engage in behavior that creates compliance risk. A group of researchers working with an insurance company asked customers to report how many miles they had driven that year, according to the odometer.[28] Reporting lower miles meant lower premiums. But instead of simply asking for the number of miles, researchers included a certification of honesty at the top of the form. Customers who certified at the top of the form, before providing their mileage number, reported almost 2,500 more miles than those who signed the same certification at the bottom of the form, despite there being no difference in driving habits.[29] The certification was effective in reducing dishonesty because it engaged morality at the moment of the decision to act ethically or unethically, just before there was an opportunity to rationalize. By triggering people's System 2 ethical monitor at the correct time, the potential for rationalization was greatly reduced. Researchers found the same type of results with tax deduction forms styled like those of the U.S. Internal Revenue Service.[30]

A similar approach can be used by companies for any expense report, conflict of interest form, or funds authorization — anything in which an employee is being asked to engage in behavior that creates compliance risk. It's up to companies to decide how high-tech they want to get. JPMorgan Chase & Co. has been developing software that monitors the actions of its traders, including emails and telephone conversations, to ensure they "adhere to 'personal trading

rules' and risk limits," and Credit Suisse Group AG is also working on technology to monitor traders' behavior.[31] JPMorgan's effort is noteworthy in that the software's algorithms can generate alerts if it appears that traders may be headed toward an ethical or legal violation. Such "predictive monitoring," like a certification at the top of a paper form, could be used by companies to intervene with a prompt before a problematic behavior occurs, forcing the employee's System 2 reasoning system to engage — and thus improving compliance.

Companies should also encourage employees to openly discuss rationalizations and how they affect ethical decision-making. This can be accomplished through storytelling by employees and the company. Employees should be encouraged, even required, to meet periodically in small groups to explore the potential effects of compliance violations and white-collar crimes. The idea is for employees, guided by compliance professionals (or, better yet, senior managers), to discuss topics such as what regulations are relevant to the business, common compliance pitfalls, and how some business practices produce externalities that negatively impact stakeholders. When rationalizing statements pop up, as they inevitably will, they should be identified and flagged. Only after patterns of self-exculpatory rationalization are openly discussed and labeled as problematic will employees be able to internalize that knowledge and use it when presented with an opportunity to act unethically.[32]

The company also should share stories of genuine compliance successes. Compliance messaging is most effective when it conveys that

positive behaviors are widely engaged in and approved of within a company.[33] The reason is related to the claim of relative normality rationalization, which allows individuals to favorably compare their potential unethical act to the unethical acts of others. Positive compliance messaging combats this rationalization by demonstrating that while there may be isolated compliance lapses, the majority of the company is committed to making ethical decisions.

One company that has used storytelling and discussions effectively in its ethics program is Parsons Corp., an international engineering and construction company based in Pasadena, California. The company hosts an internal website where it has posed hypothetical ethical problems and asked employees to vote on how they should be resolved. It then has published the narrative comments anonymously and followed up with a detailed analysis by the company's ethics committee. Such practices serve to unite employees around the company's values as applied to real-life scenarios. Through the narratives, employees themselves identify common ethical traps and rationalizations.[34] Periodically posing ethics challenges and quizzes to employees is one of a number of techniques Parsons uses in its award-winning ethics and compliance program.[35]

Use incentives to influence behavior in the right direction. Behavioral ethics research has shown that even seemingly inconsequential factors can greatly influence ethical decision-making. This is especially true when considering how rationalizations can be drawn from a company's internal culture, a large part

of which depends on incentive structures. This is one of the early lessons from Wells Fargo, where the social and monetary incentives to cross-sell products swamped the company's compliance protocols. What's more, Wells Fargo is not an isolated example; prior research has found that when major corporate trust violations occur, the root cause often has less to do with a rogue employee than with elements of the organization that are "dysfunctional, conflicting, or incongruent."[36] As a result, executives need to be aware of the common forms of rationalization described earlier in this article — and examine where in their organizations conflicting incentives could foster rationalization and wrongdoing.

To that end, business leaders can tap nonmonetary incentives to aid in compliance. According to research, praise and expressions of gratitude motivate more than money, and social group interactions motivate individual behavior more than almost anything.[37] That means the most effective compliance likely comes from something other than salary and bonus. Research also shows that compliance is most effective when employees perceive it not as a constraint but as "the governing ethos of an organization."[38] The goal, then, is for companies to build a corporate culture that incentivizes the rejection of rationalizations through the creation of shared values.

No compliance program will entirely eliminate bad employee conduct. But behaviorally cognizant programs, ones that seek to understand employee decision-making and target the cognitive mechanisms that foster unethicality, hold the promise of achieving the

primary goals of compliance: reducing unethical and illegal behavior within the company.

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Which Rules Are Worth Breaking?

Disruption of an established business model requires companies to disregard the “rules” of the status quo — within limits.

R. Edward Freeman and Bidhan (Bobby) Parmar

September 22, 2017

The 21st-century business world is being built on disruption in industry after industry. The old rules simply no longer apply to the industries being challenged: Thanks to Airbnb, for instance, hotels will never be the same; thanks to Amazon, retail will never be the same.

At one level, disruption is nothing new — simply a more modern way of rephrasing economist Joseph Schumpeter’s theory of “creative destruction.” But at another level, something else is happening. Many innovators are not just building a better mousetrap; they are also trying to articulate and consciously break the rules of the game, sometimes by figuring out ways to accomplish more with less, sometimes by finding ways around legal barriers, and sometimes by taking the low road. And there’s risk in defying too many rules.

Consider Uber. Only a few years ago, the San Francisco-based car service was the poster child for the new sharing economy. As Uber gained popularity, startups in other industries described themselves as the Uber of clothing, or food delivery, or travel reservations. Uber’s business model explored new territory, offering

customers the convenience of on-demand ride hailing via a simple app on their mobile phones. Customers got more efficient rides that were digitally integrated into their daily routines, and many of the previous hassles of getting around — from calling car services to pulling out cash or credit cards for each taxi trip to having to make ride appointments ahead of time — became a thing of the past. Uber also provided drivers the benefits of flexible work and additional income.

Uber became extremely successful in a very short time. By 2014, it was providing 1 million rides a day. By 2016, despite increasing competition, it was providing about 5.5 million rides a day globally.

But more recently, Uber has become more of a poster child for bad behavior — to its employees, its users, its communities, and the ride-hailing industry in general — as a series of mistakes and controversies began to litter its path. Earlier this year, because of its surge pricing practice on the day of protests over the Trump administration's first travel ban, more than 200,000 customers participated in a #DeleteUber campaign to stop using the app and the service. A former Uber engineer wrote a bombshell blog post a few weeks later alleging that the company repeatedly turned a blind eye to sexual harassment and had a culture of gender discrimination. Other sexual harassment issues quickly came to light: A senior vice president of engineering was forced to step down after allegations of harassment at his previous job emerged; a manager was fired for groping women at a company event; a

management team in Seoul was reported to have visited escort karaoke bars.

Uber's problems continued to ripple out. Google, an Uber investor, sued the company for stealing intellectual property from Waymo, Google's autonomous car program. Uber blamed "human error" for one of its self-driving cars running a red light and then later acknowledged that the fault lay in the self-driving system, which did not recognize the traffic lights. And after a *New York Times* report called out Uber's practice of "Greyballing" to deceive authorities in areas where the ride-hailing service was restricted, Uber brashly defended its tactics before later conceding that it would no longer use the tool.

This string of controversies led to a mass exodus of Uber senior executives, including the president, the vice president of products and growth, the head of Uber's artificial intelligence labs, and CEO Travis Kalanick himself.

Creating and executing innovative products and services that disrupt the status quo require creativity, and creativity involves thinking differently about overcoming constraints. Laws and social norms are important checks on individual and corporate behavior. But there are forces that make it tempting to push aggressively on constraints. Psychology studies have shown a correlation, for instance, between unethical behavior and creativity: Research conducted by Francesca Gino and Scott Wiltermuth demonstrates that there's a creative upside to cheating. People who cheated in one task were more likely to generate creative solutions in subsequent tasks. The researchers

credited a heightened feeling of being unconstrained by rules for the uptick.

Disruptive companies like Uber need to move from a perspective that rules and norms don't matter to a more specific understanding of *which* rules are worth breaking and why. When disrupting the status quo, smart startups would do better using a scalpel rather than a hatchet to avoid cutting off vital relationships and essential resources.

A general attitude that "the rules don't apply to us" paired with a narrow focus on outcomes (particularly shareholder value) creates fertile ground for ethical crises. While an organizational culture geared toward winning can be helpful in many ways, it can also cause unnecessary self-damage because not all rules are worth breaking — even when there is a short-term benefit. For example, society doesn't see breaking rules about taxi licenses at the same level of importance as breaking norms about respecting gender equality. When key stakeholders perceive that a good rule has been violated, they get upset and can find ways to retaliate. Eventually, the negative impressions from repeated crises accumulate and affect the brand, making it harder to attract and retain high-quality employees, customers, suppliers, and communities, all of which are necessary for the company's flourishing.

There is more to business than narrow outcomes defined as profit for shareholders. Violating rules and norms has real costs, and you have to pay for what you break.

Our own research demonstrates that employees are more likely to experience meaningful work in companies that they perceive to be pursuing an important purpose. People gain more autonomy and competence, and have better relationships, in companies they think are focused on a purpose beyond profit. This has tangible payoffs, translating to lower turnover, better employee engagement, and better customer service for companies.

Startups and other organizations that want to disrupt the status quo and also be responsible need a fine-grained understanding of which rules they want to break. Organizations need the capability to understand ahead of time the consequences of breaking certain rules, specifically understanding who will be harmed and who will benefit. Involving stakeholders in the process of developing new products and services is essential so that businesses can appreciate the stakeholders' perspectives and better identify and avoid ethical disasters. Without this capacity to anticipate and circumvent potential problems of its innovations, a company — even one with great and truly innovative ideas — can suffer a death by a thousand cuts.

Yes, we need disruption. But let's make it responsible disruption.

R. Edward Freeman is a professor of strategy, ethics, and entrepreneurship at the Darden School of Business at the University of Virginia. He tweets @re_freeman. Bidhan (Bobby) Parmar is an associate professor at the Darden School.

Ethics Should Precede Action in Machine Intelligence

A featured excerpt from *The Mathematical Corporation* by Josh Sullivan and Angela Zutavern.

Theodore Kinni

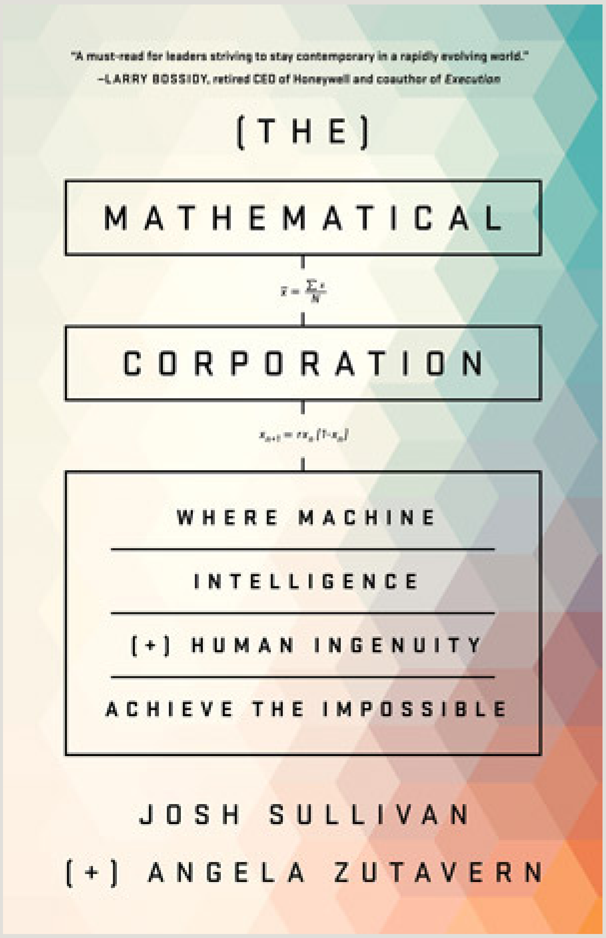
June 29, 2017

As analytics and Big Data continue to be integrated into organizational ways and means from the C-suite to the front lines, Josh Sullivan and Angela Zutavern believe that a new kind of company will emerge. They call it the "mathematical corporation" — a mash-up of technology and human ingenuity in which machines delve into every aspect of a business in previously impossible ways and produce insights that will allow previously unimaginable solutions — new businesses, strategies, products and services, and so on.

Sullivan and Zutavern don't think the mature mathematical corporation exists yet, but they do have a privileged view of the forces that will produce it. Both are executives at Booz Allen Hamilton Inc., where Sullivan organized and leads the company's data science and advanced analytics capabilities, and Zutavern is developing applications of machine intelligence to organizational leadership and strategy.

In their new book, *The Mathematical Corporation*, Sullivan and Zutavern explore how company leaders can prepare for and accelerate the transformation to a new corporate model.

The following excerpt from Chapter 7, edited for space, examines the inevitable ethical conflicts that will arise — and have already arisen — as the ability of companies to collect and parse personal data explodes. And more important, it points out the need to proactively anticipate those conflicts.



An excerpt from

THE MATHEMATICAL CORPORATION: WHERE MACHINE INTELLIGENCE AND HUMAN INGENUITY ACHIEVE THE IMPOSSIBLE

BY JOSH SULLIVAN AND ANGELA ZUTAVERN

The standard-bearer of an organization protecting personal data is the U.S. Census Bureau. Bureau chief scientist John Abowd, on leave from his professorship in economics, statistics, and information science at Cornell, cites the growing difficulty of protecting personal data in a world where people are getting better and better at re-identifying “anonymized” entries. “What was implausible in the twentieth century is now plausible,” he says.

One of the Census Bureau’s projects is the Longitudinal Employer-Household Dynamics, or LEHD, Program, which publishes trends in employment, hiring, job creation and destruction, and earnings, by geography, with data on age, sex, and industry. Abowd helped create the data set by sewing together data from the Census Bureau with other data from the fifty states. From the Census Bureau’s perspective, zero release of the core personal data is acceptable because these data include the origin and destination addresses of individual citizens as they commute to and from work.

Abowd is a leader in creating protections for such data, in particular, by modifying the data sets so that, when released, the insights from the data are correct but the personal facts have been changed so that nothing can be inferred about any individual person. The approach is called “differential” privacy, something the Census Bureau was early in using for some products in the LEHD Program. Differential privacy gives the Census Bureau the high data security the U.S. public demands.

That said, Abowd notes the tradeoff in using rigorous security: The better you protect the data, the less useful it is for decision-making. You will always face the question of how far you go in making personal data absolutely irretrievable. If, for example, you can get a big boost in public benefit by instituting a bit less rigorous protection, maybe over-the-top privacy safeguards are self-defeating. Which comes first, personal or public welfare?

“The hard question,” Abowd says, “is how do you give meaningful information while limiting the extent to which you can learn about an individual record above what can be learned from other information out there?” When it comes to weighing total protection with maximum welfare, he notes there is no technically feasible way of having all of one and all of the other.

To serve public welfare, Abowd makes sure that, despite the Census Bureau’s rigorous protections, the data remain useful. In one case, a company was thinking about expanding a manufacturing plant in rural South Carolina, but it was having second thoughts. It was worried that the targeted rural town didn’t have the five hundred skilled workers needed. But the LEHD data set showed that enough workers lived within a fifty-minute commute distance for that area. So the company enlarged its plant — and it found all the employees it needed.

Your organization may not face the rigorous privacy requirements of the Census Bureau. But the same ethical questions confront you. When is your data handling ethical and when is it not? As it turns out, in most organizations ethical

choices relate to a small number of age-old wrongs, typically forms of lying, deceiving, stealing, or harming. So when does each of these come into play in your organization? If we agree that lying, deceiving, stealing, and harming are unethical, which situations in your business become question marks?

A media lab in the Netherlands assembled a database of Dutch citizens' birth dates, professions, addresses, sexual orientations, and even medical histories using only publicly available data. How personal, private, and usable are these data? Can you ethically use it? We think not.

A Danish graduate student assembled a database of 70,000 names from the OkCupid online dating site. The list included usernames, gender, location, age, desired relationship, personality traits, and other details. In a firestorm of criticism, the student removed the data from his open repository, even as he defended the data as public and the release as ethical. Is using these data okay?

In neither of these cases do we think using the data is ethical, and let's explore why. In most cases, people set out to act ethically. But as you strive to run an organization, or build a business, or serve a government or nonprofit mission, you will always find yourself walking into gray areas. Ethical dilemmas arise, and so does the risk of making decisions you'll regret. Almost always these situations stem simply — and innocently — from temptations to make work easier, accomplish an assigned task, make extra sales, or better serve an important constituency.

Say you decide to let slide a decision that gives customers an incorrect impression about your use of their data. This is easy to do. Customers, however, might view this as you deceiving them into agreeing to unexpected uses of their data. Or say you go slow in disclosing a data breach. This also has business justifications. But your customers might perceive this as exacerbating the risk of theft of their savings. Or say you withhold data about error-prone physicians in your hospital system. Your customers, or patients, would see this as putting them at the risk of harm.

Ethical questions might reside in every task of every business, government entity, and nonprofit organization. The challenge is how to draw the line in a foggy reality. When is data brokering questionable, even if the practice is disclosed in explicit “terms of use”? When is not sharing health data a harm?

None of these are legal questions; they are ethical questions, although the law can be a guide to what society thinks about various business practices. To the extent that laws are usually the result of some issues lawmakers felt strongly about, illegal acts are usually considered unethical acts. That said, the law sets a low bar for what’s “right”; it often allows behavior that is less than what’s considered upstanding and expected.

You can use two major schools of ethical reasoning as touchstones in ethical decision-making: action based and consequence based. In action-based reasoning, whether an action is perceived as right or wrong is based on the act itself, isolated from other factors. (You would

decide deception is wrong, for instance, even if you engage in it, say, to create a better service for your customer or society.) In consequence-based reasoning, whether an action is wrong depends on future consequences: decisions that provide the greatest good for the greatest number, so-called utilitarianism, are considered ethical. (Deception is okay when you can expect, for example, that allowing hometown bias in an algorithm helps you to enlarge your community's "fair share" of state funding.)

Action-based ethics (or duty-based ethics) stem from the philosophy of Immanuel Kant. Consequence-based ethics was developed by John Stuart Mill and Jeremy Bentham. What's ethical often depends on which school of thought you side with — consciously or unconsciously — and if and when you decide to switch between the two.

If your approach is action based, then you would decide that tracking customer movements is always wrong, even if done anonymously. Period. But if you're utilitarian minded, you might instead admit that tracking is wrong, but that it does have benefits to consumers and society and so in some cases is an ethical choice. A lot of people borrow from both schools of thought, often depending on the situation, although this may do more to confuse decision-making than clarify it. The same goes for borrowing from other schools, such as "rights-based" ethics, which hold that actions are right or wrong depending on whether they violate human rights.

Whether you're on a startup journey or in an organization like the Census Bureau with

thousands of employees, management must apply ethical reasoning to arrive at ethical answers. What does your internal compass tell you? Which kind of reasoning do you feel is correct? Presuming you follow the law, you still have to clarify your ethical philosophies and those on which your organization stands.

What are the big areas you should be thinking about? We urge you to think of the following four and decide on your ethical reasoning in handling ethical questions in advance:

- Transparency in data handling
- Protection of privacy
- Data ownership
- Data security

In the journey to becoming a mathematical organization, applying ethical reasoning in advance is not an exercise to perfect your ethics just to feel good about yourself. It is an exercise of introspection that improves your strategic decision-making to prevent mistakes.

Theodore Kinni is a contributing editor for *MIT Sloan Management Review*. He tweets @tedkinni.

Why the Business Case for Sustainability Will Win Out

The Trump administration's dismissal of U.S. climate promises casts a shadow over climate change commitments by the country. But U.S. corporations still have considerable incentive to move forward on their own plans, despite the softening of government support.

Leslie Brokaw

June 28, 2017

Last summer, the beer company Anheuser-Busch temporarily rebranded its iconic Budweiser cans by plastering the word "America" across them instead of the word "Budweiser." Nothing says "I love the U.S.A." like a clever marketing campaign, right?

In fact, Anheuser-Busch has another program that sells its passion for this country in a more concrete and more profound way: It's called the Better World campaign, and it has resulted in the company's reduction of water use at its U.S. breweries by almost 50% over the past 10 years, recycling of 99.8% of its waste at the same facilities, and scaling back on its packaging materials by more than 75,000 tons. Three months ago, Anheuser-Busch went a step further and announced it would purchase 100% of its electricity from renewable sources by 2025 — an act it estimates will make it the largest corporate direct purchaser of renewable electricity in the global consumer goods sector.

Then Donald Trump declared that he would withdraw the United States from the 2016 Paris climate agreement. The United States had reiterated in that global accord that it was targeting a reduction of U.S. greenhouse gas emissions by 26% to 28% below 2005 levels by 2025.

Anheuser-Busch's reaction? Chief sustainability and procurement officer Tony Milikin reaffirmed the company's climate commitments. "Fossil fuels contribute directly to climate change," he wrote, in a column published the same day as Trump's statement. "By initiating long-term agreements with clean-energy providers, businesses can provide stable demand and the capital for further investment in local renewable energy infrastructure projects." Buying renewable energy makes good business sense, Milikin added: "In some markets, renewable energy purchased via PPAs [power purchase agreements] is cheaper than grid-sourced electricity."

Milikin's comments may not have been designed as a direct rebuke to the president, but they essentially said that Anheuser-Busch remains fully committed to climate efforts because it's (1) good for America and (2) economically smart for the company.

Anheuser-Busch is not an outlier. More than 1,200 U.S. governors, mayors, and businesses have signed an open letter pledging that "We Are Still In." Apple, Campbell Soup, General Electric, Facebook, Tesla, and Walmart have all said that they will continue with company-specific plans to battle climate change.

MIT Sloan Management Review has been investigating sustainability's business case for years. Our new report, "Corporate Sustainability at a Crossroads," points out that adjusting a company business model to capture sustainability opportunities "will work in the long term only if one can establish a business case for these efforts." How and why companies make that case has been a recurring theme in our eight years of examining how climate action is becoming corporate policy. Here are some of the stories we've highlighted:

- Our 2011 sustainability report noted that institutional investors, such as universities and state pension plans, are providing motivation and incentive, by demanding more information on companies' sustainability performances. Roberta Bowman, then senior vice president and chief sustainability officer of Duke Energy Corp., the Charlotte, N.C.-based electric utility company, said: "In addition to the more traditional 'socially responsible investors,' we are finding that some of our mainstream investors are now looking at sustainability performance as an indicator of overall business value. They're acting on the theory that our sustainability measures — our efficiency with resources, our employee retention, etc. — are predictors of overall business profitability." Today Duke, through its Duke Energy Renewables LLC subsidiary, acquires, develops, and operates wind and solar renewable generation in 14 states across the United States.
- Footwear and apparel company Timberland LLC, based in Stratham, New Hampshire, was working closely with the U.K.-based auditing organization Leather Working Group when we talked to Betsy Blaisdell, manager of environmental stewardship for Timberland, for our 2014 sustainability report. The auditing group maintains a protocol that assesses the environmental compliance of tanners and promotes sustainable environmental business practices within the leather industry. "Through our work with the group, we can foster best practices related to energy, chemical, and water management, and make sure we only buy from silver- or gold-rated tanneries," said Blaisdell. "The work also reduced complexity in sourcing." Today, Timberland uses an index that measures the climate impact, chemicals, and resources consumed in the manufacture of some of its footwear products. The index helps the company compare

a product’s score with its profit margin. Sustainable products “may be more expensive to produce, but generate better margins,” said Blaisdell.

- Stonyfield Farm Inc. remade part of its supply chain to help ensure access to organic bananas, an important part of its product mix. Wood Turner, then the company’s vice president of sustainability innovation, told us in 2014 that the New Hampshire yogurt company had for years been purchasing the pesticide-free fruit from an excellent Costa Rican grower association. But the association relied on contract processors to turn the bananas into puree, and that part of the process had a lot of instability. The situation, said Turner, affected the growers’ ability to see significant margins and Stonyfield’s “security of supply, which creates all kinds of challenges for us.” Stonyfield’s solution was to collaborate with the grower association “to disrupt their business model by installing small-scale processing capability.” The growers became processers as well as farmers – allowing them to sell directly into the global marketplace and stabilizing Stonyfield’s supply chain at the same time. Stonyfield still touts this collaboration on its online Source Map, which details who’s producing its ingredients.

The bottom line: Sustainability efforts that make corporate operations more stable and are financially profitable have built-in incentives for companies to remain committed to them. That will continue to be true — whether the U.S. is a party to the Paris agreement or not.

We invite you to explore our sustainability reports and interviews from over the years, and read our new sustainability summary about all the ways that corporations are battling climate change today.

Leslie Brokaw is a contributing editor to *MIT Sloan Management Review.*

Corporate Sustainability at a Crossroads: Progress Toward Our Common Future in Uncertain Times

In the final report of our eight-year study of how corporations address sustainability, *MIT Sloan Management Review* and The Boston Consulting Group examine the crossroads at which sustainability now finds itself. Despite sociopolitical upheaval that threatens to reverse key gains, our research has shown that companies can develop workable — and profitable — sustainability strategies to reduce their impact on the global environment by incorporating eight key lessons.

David Kiron, Gregory Unruh, Nina Kruschwitz, Martin Reeves, Holger Rubel, Alexander Meyer Zum Felde

May 23, 2017

Executive Summary

MIT Sloan Management Review and The Boston Consulting Group have been tracking corporate sustainability for the past eight years, surveying tens of thousands of managers and interviewing more than 150 executives and thought leaders, while producing eight annual reports and numerous blogs and articles. *MIT SMR* and BCG joined forces to increase knowledge about business adoption of sustainable practices and to support the integration of sustainability into

business strategy. (See Appendix for summaries of the reports.)

Despite significant progress, corporate sustainability has arrived at a crossroads. In one direction, corporate leaders in sustainability remain a minority, and are unevenly distributed across geographies and industries. In the other direction, a handful of standout companies are demonstrating that sustainability can be a driver of innovation, efficiency, and lasting business value. Populist political movements around the world threaten to set back global diplomatic progress on issues like climate change and reverse recent regulatory trends. All of this complicates the calculus of corporate leaders and their sustainability strategies.

Key Lessons

Key Lesson #1: Set your sustainability vision and ambition: 90% of executives see sustainability as important, but only 60% of companies have a sustainability strategy.

Key Lesson #2: Focus on material issues: Companies that focus on material issues report up to 50% added profit from sustainability. Those that don’t focus on their material issues struggle to add value from their sustainability activities.

Key Lesson #3: Set up the right organization to achieve your ambition: Building sustainability into business units doubles an organization’s chance of profiting from its sustainability activities.

Key Lesson #4: Explore business model innovation opportunities: Nearly 50% of

companies have changed their business models as a result of sustainability opportunities.

Key Lesson #5: Develop a clear business case for sustainability: While 60% of companies have a sustainability strategy, only 25% have developed a clear business case for their sustainability efforts.

Key Lesson #6: Get the board of directors on board: 86% of respondents agreed that boards should play a strong role in their company's sustainability efforts, but only 48% say their CEOs are engaged, and fewer (30%) agreed that their sustainability efforts had strong board-level oversight.

Key Lesson #7: Develop a compelling sustainability value-creation story for investors: 75% of executives in investment companies think sustainability performance should be considered in investment decisions, but only 60% of corporate executives think investors care about sustainability performance.

Key Lesson #8: Collaborate with a variety of stakeholders to drive strategic change: 90% of executives believe collaboration is essential to sustainability success, but only 47% say their companies collaborate strategically.

Fortunately, the path to sustainable value creation has become substantially clearer in the past eight years. Based on our multiyear research on corporate sustainability, we have identified eight evidence-based factors that drive sustainable business practices, regardless of industry or region:

1. Articulate a practical sustainability vision and ambition that lays the foundation for new business practices.
2. Identify and prioritize material issues to focus resources.
3. Embed sustainability organizationally through cross-functional teams, clear targets, and key performance indicators (KPIs).
4. Innovate on multiple dimensions of your business model.
5. Develop a clear business case.
6. Get the board of directors on board.
7. Communicate a sustainability value-creation story to your shareholders.
8. Collaborate with a variety of stakeholders to drive strategic change.

In this report, we draw upon our database of more than 60,000 survey respondents from companies around the world to assess the emergence of corporate sustainability across industries and elaborate the above eight critical insights that can help executives accelerate their company's contribution to our common future.

Introduction

This year marks the 30th anniversary of the publication of "Our Common Future,"[1] the report from the United Nations World Commission on Environment and Development (also known as the Bruntland report) that launched the idea of "sustainable development." The report envisioned a future where current economic prosperity did not come at the expense of future generations. But its definition of sustainability as "development that meets the needs of the present without compromising the ability of future generations to meet their own needs" was diplomatic sleight-of-hand, cleverly satisfying both economic and environmental ministers but offering no guidance on how such a vision might be implemented.

The research and analysis for this report was conducted under the direction of the authors as part of an MIT Sloan Management Review *research initiative in collaboration with and sponsored by The Boston Consulting Group.*

Three decades in, we have yet to implement this vision. However, today we know much more about what it will take to make it real. We know, for example, that relying only on government fiat to address sustainability issues such as climate change, water scarcity, depletion of natural resources, and workers' rights is insufficient. Many solutions lie with business and the commercial sector's ability to innovate. Sustainable corporate performance is essential, and executive leadership vital. Proactive action from the private sector is now recognized as fundamental to realizing a sustainable future.

Today's business leaders demonstrate a much higher level of commitment to corporate sustainability than existed when the Brundtland report was published back in 1987. Nine thousand companies have joined the UN Global Compact since it was established in 2000.[2] Its members commit to 10 sustainability principles. Seventy-four percent of the world's largest companies now use the Global Reporting Initiative's process for tracking and reporting their sustainability performance.[3]

In practice, a majority of executives today agree that having a sustainability strategy is necessary to be competitive.[4] More and more companies are reporting on their sustainability performance.[5] The roster of businesses with multibillion-dollar sustainable business practices is expanding year by year.[6] Corporate

sustainability is no longer a marginal or money-losing set of activities.[7]

A vast network of tool makers, including investors, consumer groups, organizations, coalitions, certifiers, and platforms, now exists to spur and aid sustainable business practices. Two significant trends have emerged in relation to this burgeoning network: One is that companies, as well as partners in their value chain, have become much more transparent about their own sustainability-related activities. Corporations are doing more to track and communicate sustainable practices, just as more tools have become available to consumers and non-corporate actors to measure and monitor (un)sustainable business activities. Notably, social media and other technology platforms have become effective mechanisms for heightening awareness of crises and corporate misbehavior, exerting increased pressure on companies to respond.

A second trend relates to groups of companies or nations working together to forge new standards and goals for sustainable business practices. The Sustainability Consortium, for example, founded nearly a decade ago with funding from Wal-Mart Stores Inc., has a significant network of members committed to science-based sustainability guidelines for products and supply chains. Just last year, representatives of 195 countries ratified a landmark climate agreement in Paris to set nation-by-nation limits on greenhouse gas emissions beginning in 2020. Signatories to the agreement represent a large portion of the world’s population. The Paris Agreement will likely have a significant impact on the global

economy and focus sustainability practices in industries around the world. Even with a climate skeptic at the helm of the executive branch of the U.S. government and uncertainty about whether the United States will withdraw from the treaty, large polluting nations like China and India have begun introducing stricter regulations in accord with the Paris Agreement.

THE CROSSROADS

Despite this progress, corporate sustainability has arrived at a crossroads. In one direction, corporate leaders in sustainability remain a minority and are unevenly distributed across geographies and industries. Stand-out corporate leaders, like Unilever's Paul Polman or Patagonia Inc.'s Yvon Chouinard, are still the exceptions. In another direction, the natural environment continues to change as a result of human activity. Catastrophic loss events from naturally occurring events like floods, earthquakes, and droughts are becoming more frequent and intense,[8] threatening regional economies and compounding resource-scarcity issues that afflict many areas. In still another direction, global economic inequality presents a growing risk to globalization and international market stability.

Public attitudes toward government regulation and efficacy also intersect with corporate sustainability. With populist and anti-regulatory leaders on the rise, trust in government institutions reaching a low point, and some political leaders denying the reality of climate change, the potential for corporate sustainability to lose momentum or backslide is all too real. In the United States, the coal industry is undergoing a wave of deregulation,

prompting concerns that the U.S. will displace China and reclaim its title as the world's largest emitter of greenhouse gases. Elsewhere, deforestation rates in the Amazon rainforest are on the rise after a decade of declines, pointing to the potential for broad reversals in recent trends.[9]

If backsliding is to be avoided, corporate leaders have an urgent need to accelerate their sustainability efforts and resist the siren song of new anti-regulatory incentives that tempt leaders to scale them back.

What can corporations do to hasten their sustainability efforts? A first step is to better understand the progress corporate sustainability has already made, and then build on those lessons. *MIT Sloan Management Review* and The Boston Consulting Group have been tracking developments in corporate sustainability for the past eight years, surveying tens of thousands of managers and interviewing hundreds of executives and thought leaders, while producing eight annual reports and numerous blogs and articles. (See Appendix for summaries of the reports, in addition to links.) For this report, we assess the emergence of corporate sustainability across industries, and elaborate eight critical insights about what executives can do to accelerate their company's contributions to our common future.

Corporate Sustainability Hits the Mainstream

To see how far corporate sustainability has come, one need look no further than the financial sector. Think of the financial sector as

a group of organizations that includes not only retail and commercial banks but also central banks, insurance companies, re-insurance companies, asset management companies, investment funds, venture capitalists, private equity companies, institutional investors, and stock exchanges.

In 2010, a UN-financed report revealed that only 22% of 766 CEOs believed that the investment community would be major stakeholders in their company's sustainability efforts.[10]

No more.

Our 2016 report, "Investing for a Sustainable Future," demonstrated that a clear majority (60%) of executives in publicly traded companies believe that good sustainability performance is important to investors. But even this majority understates how much investors really care about corporate sustainability. Our survey results show that an overwhelming three-quarters (75%) of senior executives in mainstream investment firms believe sustainability performance is materially important to their investment decisions. Seventy-four percent of surveyed investors agreed that sustainability performance matters more than it did three years ago. Investors care more about sustainability than many managers believe.

A 2016 report from the Morgan Stanley Institute for Sustainable Investing and Bloomberg LLC shows that among 402 asset managers, 89% were familiar with sustainable investing and 65% practiced sustainable investing in some

form.[11] Bob Eccles, retired Harvard Business School professor and chairman of Arabesque, a London-based investment company, observed, "The vice chairman of one of the top 10 banks by market cap told me he interviewed all 50 of their largest institutional investors last year, and that was the first time every single one asked about sustainability or ESG. Companies have been complaining for years that nobody cares about sustainability, but investors care, and companies need to up their game."

Many efforts are underway to guide companies on how to report environment, social, and governance (ESG) metrics. Below are three examples of organizations that address this:[12]

- The United Nations-supported Principles for Responsible Investment (UN PRI) state that an "economically efficient, sustainable global financial system is a necessity for long-term value creation" and will reward long-term responsible investment. More than 1,600 investment organizations have committed to the UN PRI's six principles of responsible investment, which include incorporating ESG issues "into investment analysis and decision-making."[13]
- In the U.S., the Sustainability Accounting Standards Board (SASB) is working to develop rules governing public disclosure of financially material corporate sustainability information. SASB's stated mission is to develop and disseminate sustainability accounting standards that help public corporations disclose material, decision-useful information to investors.[14] SASB is developing a materiality matrix that identifies key sustainable issues for companies in 79 industries and 10 sectors. SASB claims to be the only sustainability standard to cover 79 industries.[15]
- The UN's Sustainable Stock Exchange Initiative, established in 2009, works with stock exchanges to develop more sustainable capital markets. According to a 2016 report on the Initiative's website, "More than 70% of listed equity markets — 58 stock exchanges altogether — have signed on. Twelve exchanges incorporate reporting on ESG information into their listing rules, and 15 provide formal guidance to issuers."[16]

Many new analytics tools and platforms are making ESG performance information easier to access — and make sense of.[17] This trend toward better access to better data is expanding the group of stakeholders using information about corporate performance on ESG factors, including millennials looking for employment opportunities with companies that have strong sustainability performance.

Investors are not just looking for information; they are also looking for new sustainability-oriented investment products. A 2016 *Wall Street Journal* article, "'Sustainable Investing' Goes Mainstream," documents the trend, discussing new sustainability products from BlackRock and Goldman Sachs.[18] Likewise, the emergent labeled green bond market is expanding rapidly, reaching $118 billion in 2016.[19] Green bonds are debt issuances that meet certain international standards ensuring projects will have a positive environmental impact: They represent a growing, but still tiny, fraction of the overall global bond market, which has a value close to $90 trillion.[20] Indeed, all new multi-decade bond issuances are being increasingly scrutinized through a sustainability lens. With such long payback periods, lenders need to know that a borrower's business can be sustained in an increasingly hot, crowded, and uncertain world.

Even with the proliferation of information, tools, products, organizations, and networks aimed at advancing or exploiting corporate ESG conduct — along with heightened awareness among executives and public interest in corporate sustainability — the advancement of sustainable business practices within companies is irregular

across industries, geographies, and company size.

Uneven Progress

Companies that are leading the corporate sustainability movement have many things in common, but a fundamental one is having a *sustainability strategy*. Sustainability strategies are not created equal, however, and their relevance to core business activities varies widely among organizations. Since every company has a unique organizational structure, supply chain, employee base, geographic footprint, and so on, it is logical that every company also has a unique sustainability profile. This makes variety in sustainability strategies inevitable. Some managers will say they have a sustainability strategy, but often it's just a near-term plan for achieving incremental environmental or social improvements or complying with relevant existing regulations. For other companies, sustainability strategy is linked to their overall business strategy, often encompassing the supply chain and customer segments. In the most advanced companies, sustainability strategy *is* the business strategy, fully embedded in the company's purpose. We discuss differences between these strategies below.

Key Lesson #1: Set your sustainability vision and ambition:

90% of executives see sustainability as important, but only 60% of companies have a sustainability strategy.

Figure 1: The Importance of a Sustainability Strategy

Ninety percent of respondents see sustainability as important, but only 25% have developed a positive business case.

Corporate leaders in sustainability not only articulate a vision for their sustainable business but also connect that vision to a strategy. Although 90% of managers agree that having a sustainability strategy is important to their business, only 60% claim that their organization has any kind of sustainability strategy (see Figure 1). Many companies have no real sustainability strategy at all. Instead, they have projects, anecdotes, and examples they make available to shareholders, regulators, and consumers in the form of glossy sustainability reports. Our research indicates that companies struggle to find a payoff from sustainability until they develop a true sustainability strategy and

build a solid business case. Dave Stangis, vice president of public affairs and corporate responsibility at Campbell Soup Co., explains that many companies are not acting strategically and haven't figured out how to really integrate sustainability. "They are throwing things against the wall to see if they stick," he says. "They probably are losing money on sustainability."

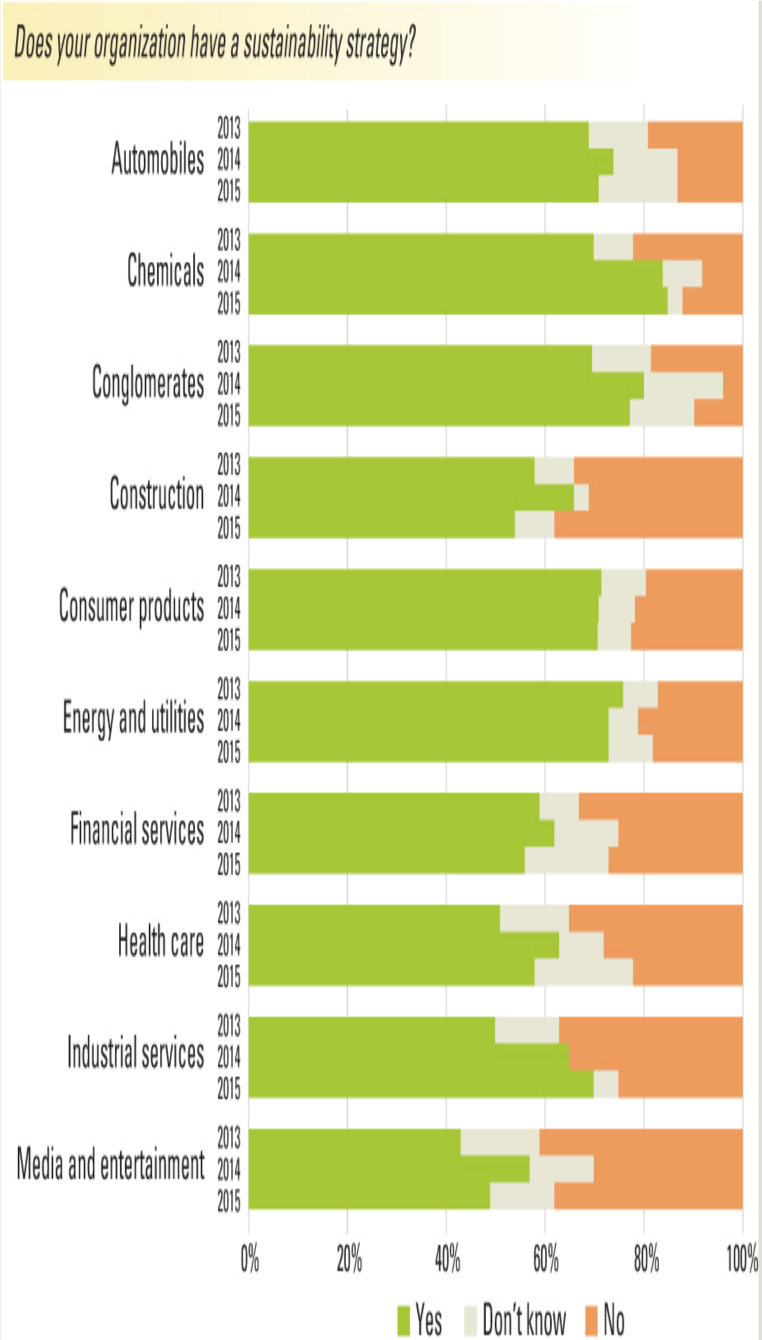


Figure 2: Organizations With Sustainability Strategies by Industry

Highly regulated industries such as energy and utilities are most likely to have a sustainability strategy.

UNEVEN PROGRESS ACROSS INDUSTRIES

Industries that have the highest percent of companies with a sustainability strategy are in chemicals, energy and utilities, industrial goods and services, and machinery (see Figure 2). These, of course, are highly regulated industries with substantial environmental and health and safety concerns, as well as significant resource needs or constraints. Sustainability issues are an inescapable aspect of these industries, with many concerns becoming material to the success (and failure) of their businesses. For companies in these industries, having a sustainability strategy is practically mandatory. In the energy sector, for example, oil and gas companies often need to address environmental and social factors in order to meet the expectations of communities in their operating and market environments; a broader strategic approach to sustainability that embraces more of their business is a necessity. “For us, this is a key part of the business driver behind sustainable development,” says Tom Albanese, CEO of Rio Tinto. “It is the license for our asset base to operate.” Some sectors within the energy industry may not survive as pressures mount to move toward a less carbon-dominated economy. For companies in the coal sector, for instance, a sustainability strategy might mean shifting their corporate focus away from coal products. (See Sidebar: Sustainability For Some, But Not Others.) With the United Kingdom prohibiting the use of coal plants after 2025, Drax, a power company, is moving aggressively to transform its coal plants into wood pellet-burning plants and to increase its wind and solar energy capacity.[21]

Sustainability For Some, But Not Others

In a sustainable future, some industry sectors may not survive. According to London Business

School professor Ioannis Ioannou, the possibility that some companies may not make it in a sustainable future “is quite expected.” He explains, “In my mind, the pressure for sustainability is, in many ways, the mother of all disruption. We’re talking about challenges that go far beyond just technological innovation in terms of products and services. We’re talking about business model innovation. We’re talking about changing the very identity of organizations… It will be no surprise that a lot of companies will simply fail to meet that expectation.”

In general, corporate lifespans are shrinking; publicly traded companies in the U.S. have a 1 in 3 chance of disappearing in the next five years, a sixfold increase since 1965.[i] It’s a broad-based phenomenon: Most types of businesses in most industries run the risk of dying younger. Sustainability is just adding additional pressure to this trend.

PROGRESS VARIES BETWEEN GEOGRAPHIES

The share of companies with sustainability strategies varies across regions. The percentage of companies with a sustainability strategy has steadily increased in Australia, Europe, and Latin America (see Figure 3). Unsurprisingly, businesses that operate in multiple regions have the highest share of sustainability strategies. Northern America[22] has a relatively low proportion of organizations with sustainability strategies, and there is a significant risk that the deregulation push of the current U.S. administration could unravel the social and environmental gains of the last few years. Companies in both North and Latin America are less likely to view sustainability-oriented

strategies as necessary to be competitive (see Figure 4).

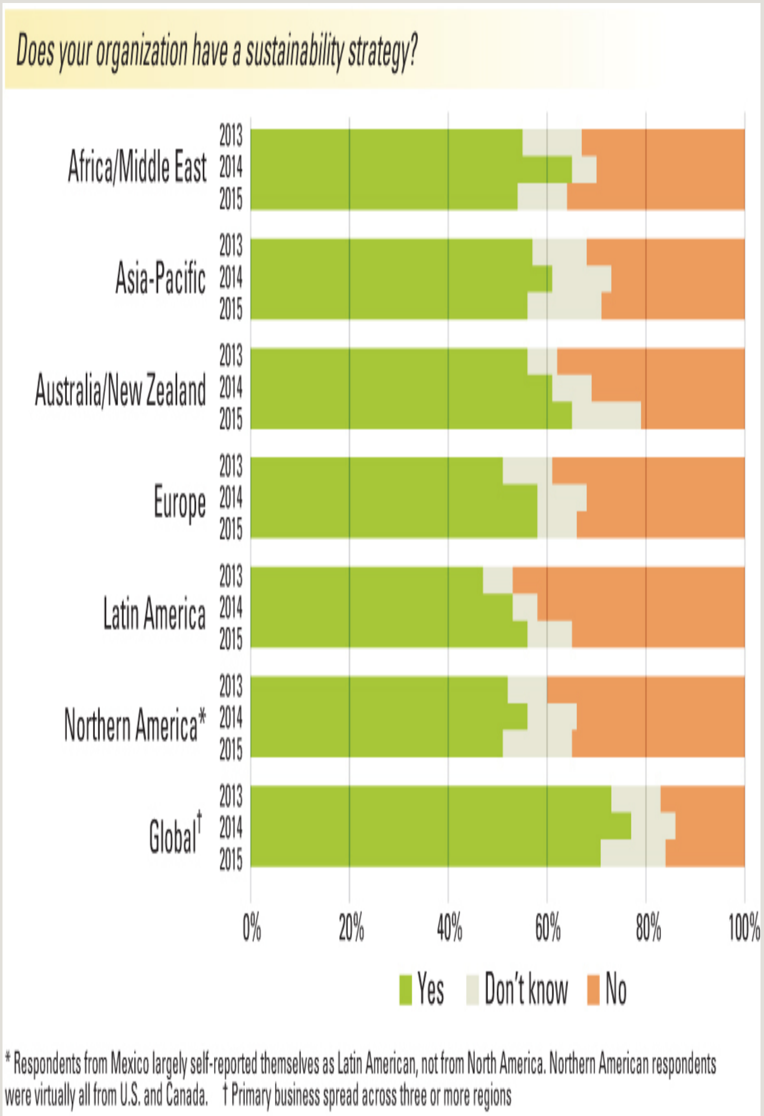
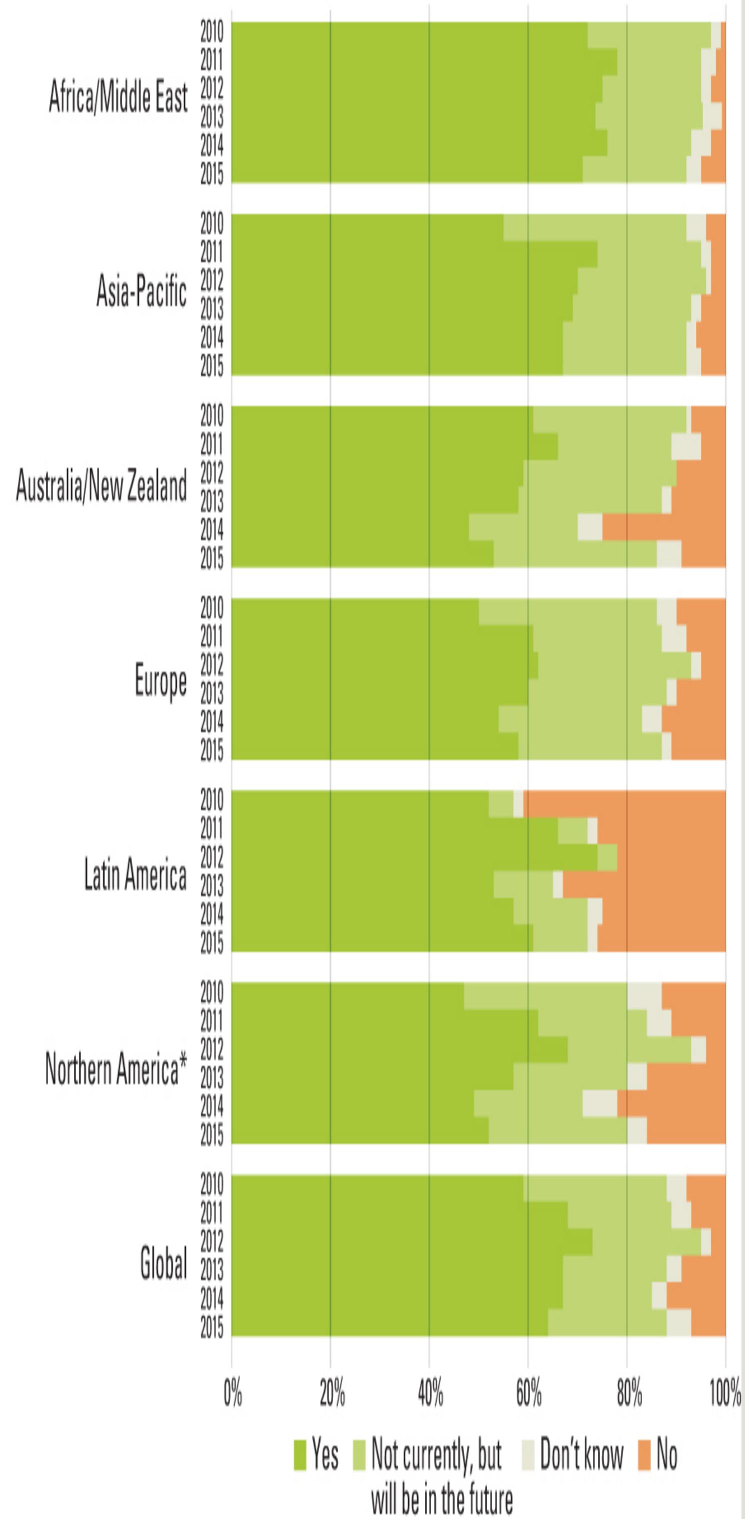


Figure 3: Organizations With Sustainability Strategies by Region

Companies in Northern America are less likely to have sustainability strategies.

Is pursuing a sustainability-oriented strategy necessary to be competitive?



* Respondents from Mexico largely self-reported themselves as Latin American, not from North America. Northern American respondents were virtually all from U.S. and Canada.

Figure 4: Competing With Sustainability

Percent of managers who perceive sustainability-oriented strategies as necessary to be competitive varies by region.

Internal or external forces may drive adoption of a sustainability strategy. In Latin America, for instance, external pressures in the form of new regulatory policies are driving adoption of sustainability strategies in the mining industry. Mining incidents and popular protests are spurring regional governments to strengthen the criteria that companies must meet in order to obtain, and maintain, their license to operate. In other Latin American industries, strong leadership motivates adoption of sustainability strategies. The Costa Rican beverage leader Florida Ice & Farm Co. SA is a case in point. In 2005, the company responded to Costa Rica’s looming water access crisis by investing in water-saving measures. Within two years, the organization had decreased its use of water in production by an eye-popping 82%, becoming Latin America’s first water-neutral company in 2012. Beyond the sustainability gains, the reduction drove down production costs and helped sustain 20% annual growth between 2010 and 2014.[23] Gisela Sanchez Maroto, director of corporate relations at Florida Ice, explains, “We found reasons — even business reasons — to have an environmental and sustainability strategy.”

In general, many of the organizations from Latin American and Asia-Pacific countries that are represented in our survey are in countries such as Brazil, Colombia, Indonesia, and India, where

ESG factors are significant features of the market environment.

PROGRESS VARIES RELATIVE TO SIZE

The largest companies in our database (100,000 or more employees) have consistently been the best performers across a range of metrics. “The big organizations are not only good at problem-solving but also at scaling up sustainability solutions,” says Ioannis Ioannou, associate professor of strategy and entrepreneurship at London Business School. The largest companies are most likely to have a sustainability strategy: 78% of large companies do versus 54% of small companies (10,000 or fewer employees). They are also most likely to report that sustainability has been a top priority for management. Moreover, the share of large organizations that have changed business models because of sustainability innovation is greater than those of both midsize (10,000 to 100,000 employees) and smaller companies.

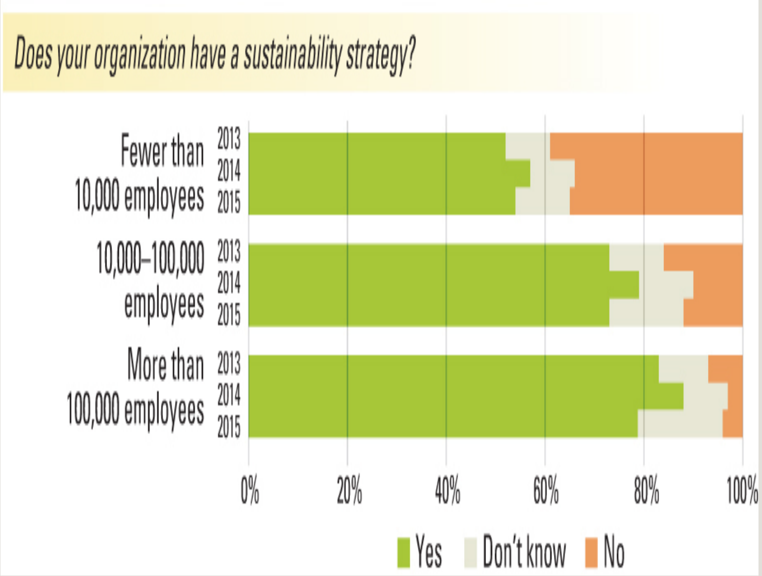


Figure 5: Organizations With Sustainability Strategies by Size

Larger companies are more likely to have a sustainability strategy.

As Figure 5 illustrates, size matters, and it's not a surprise that large global operators are much more likely to have a sustainability strategy in place. Many large companies are looking to emerging markets for growth, and those markets can be rife with sustainability-related issues.[24] Multinational organizations operating in global markets often find it easier to develop a consistent compliance approach by applying the regulatory standards of the most stringent countries to all of their operations, regardless of location. Doing so raises the bar for sustainable business practices in all of the markets where the company operates.

Unilever is a prime example. When top management conducted a review of its overall business, Unilever executives realized that the company's future growth would come from emerging markets that had significant sustainability issues in areas like deforestation, poor sanitation, and water scarcity.[25] The company subsequently analyzed its entire value chain across brands and countries and discovered that "much of its footprint was at the consumer end, involving issues such as using more product than necessary or improper end-of-life disposal."[26] This discovery gave the senior leadership team a purpose and a rationale for aligning its resources behind a strategic sustainability focus. In 2016, the company's Sustainable Living brands were growing 30% faster than its traditional brands.[27]

One takeaway from the performance of the largest companies is that there is an excellent opportunity to improve the sustainability performance of smaller corporations. Mindy Lubber, CEO of CERES, a Boston-based nonprofit that works with business on developing their sustainability agendas, notes: “We have to focus on midsize companies and smaller companies because they have equally compelling opportunities, but they’re just not as far along.”

PROGRESS: A WORK IN PROGRESS

The uneven distribution across industry, geography, and size of companies with sustainability strategies is a call to action, especially for the 40% of companies in our surveys that don’t have a sustainability strategy.

A major constraint for those organizations is that their leadership tends to view ESG factors as necessary issues to address, rather than as sources of business opportunity. In contrast, companies with more developed sustainability strategies view sustainability as both a necessity and an opportunity — what PepsiCo’s senior director of sustainable development, Dan Bena, calls the sustainability bull’s-eye.

“It requires rethinking how to do things,” says Andrew Hewitt, founder of GameChangers 500, an organization that ranks the world’s top “for-benefit” businesses. Incremental change and eliminating externality risks are not enough to produce meaningful results. “You check the boxes by recycling and composting to reduce harm; however, you change the game when you redefine success and build your business

operations to meet new measurements of value," he explains.

Making Material Progress

Companies with successful sustainability strategies connect their sustainability efforts with issues and activities that are material to the business. "Strategies" that focus on biking programs, recycling drives, or a CEO's pet philanthropy have little impact on the business and the larger sustainability issues that matter most. These are not strategies for making the business sustainable over time. "If you're a bank and you've got an energy-savings program and you're in LEED platinum buildings, investors aren't going to care," says Arabesque's Eccles. "But if the bank's loan portfolio has a bunch of ESG risk and stranded assets … those are things that are material."

Patagonia Inc. is an example of a company that connects its sustainability strategy with material business issues. As a leading textile manufacturer and retailer, Patagonia recycles plastic waste into its innovative fabrics and, with its Worn Wear motto, "Better than new," encourages its customers to mend and repair Patagonia clothing rather than throwing it out and buying new.[28] From 2008 to 2015, Patagonia had a compound annual growth in revenues of 14%, while profits surged 300% during this period. It also contributes 1% of annual revenues to nonprofit organizations that promote conservation of the natural environment their outdoor customers love.[29]

Key Lesson #2: Focus on material issues:

Companies that focus on material issues report up to 50% more profits from sustainability activities than those that do not. Those that don't focus on their material issues struggle to add value from their sustainability activities.

In some cases, external stakeholders encourage the company to make the materiality connection. Consider Greif Inc., a supplier of industrial packaging products, such as large steel drum shipping containers, to businesses in over 50 countries. Many of Greif's customers were shifting their priorities from buying shipping containers to seeking a sustainable "shipping solution" that would help reduce emissions in their value chain. In the mid-2000s, more customers began asking Greif managers for environmental information, such as greenhouse gas emissions data. In response, the organization began lifecycle analysis (LCA) studies on its core products of steel, plastic, and fiber containers.[30] The analyses showed that the most effective way to improve the environmental performance of its containers was to make the containers heavier, longer-lasting, and easier to reuse. This result surprised Greif managers, who expected lighter or thin-gauged containers to be the most environmentally sound solution. Based on this discovery, Greif determined that its core business should strategically shift toward reconditioning containers and related services. The LCA studies helped Greif identify strategic environmental risks in its value chain and develop a successful strategy for integrating additional sustainability services into its business model.

BASF Accelerates Its Approach to Sustainability[ii]

BASF's accelerators program aims to turn all products into sustainability all-stars. The business case is solid for creating these highly sophisticated, sustainability-centered products. Accelerator products account for 10 billion euros [$11B], or almost 18% of the company's total annual relevant product sales of 56 billion euros [$61.6B]. To ensure that the message of each product's sustainability benefits reaches customers, the BASF sales force has a product card that describes each product's sustainable characteristics, such as recyclability or reduction of water use in manufacturing.

The program is the fruit of a carefully planned approach to engaging BASF's board. The company established a steering initiative for sustainable solutions that combined a "top-down" perspective — driven by a sustainability board chaired by a member of the board of directors — with a "middle-out" perspective, in which every business unit assesses its own products against strict sustainability criteria.

The sustainability board then went to the business units to secure buy-in from their leaders and draft strategies for making needed changes. Armed with business-unit specifics and challenges, the sustainability board next returned to the board of directors and presented its findings. It got a green light to conduct deep dives into core businesses and create a "sustainable solutions approach" (the accelerators program) that would encompass every product line in the company. Identifying business and sustainability risks within business units allowed BASF to create market solutions that would not have happened otherwise.

BASF SE, the German chemicals giant, takes a more proactive approach. Several years ago, executives began reassessing the company's entire business model through a sustainability lens. (See Sidebar: BASF Accelerates Its Approach to Sustainability.) By 2014, the company had assessed 80% of its product portfolio — some 50,000 product applications — on a sustainability scale that ranks whether a product is exceeding, meeting, or noncompliant with certain sustainability standards.[31] At the top of the rankings are "accelerator" products. These sustainability all-stars make a significant contribution to the market and exceed environmental and social standards for the product category. BASF has identified 13,500 accelerator solutions in its sales portfolio. "Performer" products meet basic market standards and are followed by "transitioners," which are products actively addressing sustainability issues. At the bottom of the list are "challenged" products that carry significant sustainability risks. Product teams develop plans to move their products up the ranks.

BASF's reassessment of its products, and subsequent overhaul of its business, is an essential feature of its mission to "create chemistry for a sustainable future," which has full support from the CEO. The entire effort of reviewing the business through a sustainability lens was vetted by a council of business line presidents and eventually sanctioned and supported by the company's board.

Our 2013 report, "Sustainability's Next Frontier," offers evidence that 52% of companies that mostly or completely address their material sustainability issues also profit from their

sustainability strategies. In contrast, only 16% of companies that pay little or no attention to material issues report that they profit from sustainability. Although some sustainability concerns are common within a given industry, material sustainability issues vary by industry. SASB’s Materiality Map tool helps companies identify relevant material issues common to their respective industries.[32]

Key Lesson #3: Set up the right organization to achieve your ambition:

Building sustainability into business units doubles an organization’s chance of profiting from its sustainability activities.

INNOVATE THE BUSINESS MODEL

The previous examples offer anecdotal evidence of the strong connection between successful sustainable strategies and significant change to business models. Our survey data also offers robust quantitative evidence for this connection. In the survey for our 2013 “Innovation Bottom Line” report, we asked respondents to use the business model framework below to identify which parts of the business model they were changing in response to sustainability factors.

VALUE PROPOSITION What are we offering to whom?	OPERATING MODEL How do we profitably deliver the offering?
• Target Segments • Product or Service Offering • Revenue Model	• Value Chain • Cost Model • Organizational Change

A surprising combination of business model elements delivered the most potent results. It wasn't the game-changing products and businesses that one usually hears about in the context of innovation that drove sustainability value. It was the combination of innovation in the value chain and target segments that provided the strongest link: We found that 59% of companies that profited from sustainability by changing three or four business model elements pulled these two levers (see Figure 6). They often go hand in hand to boost bottom lines. Changing the business model without a proper strategy, or effective leadership and organizational change, however, will not lead to desired results, and could backfire without a shift in culture.

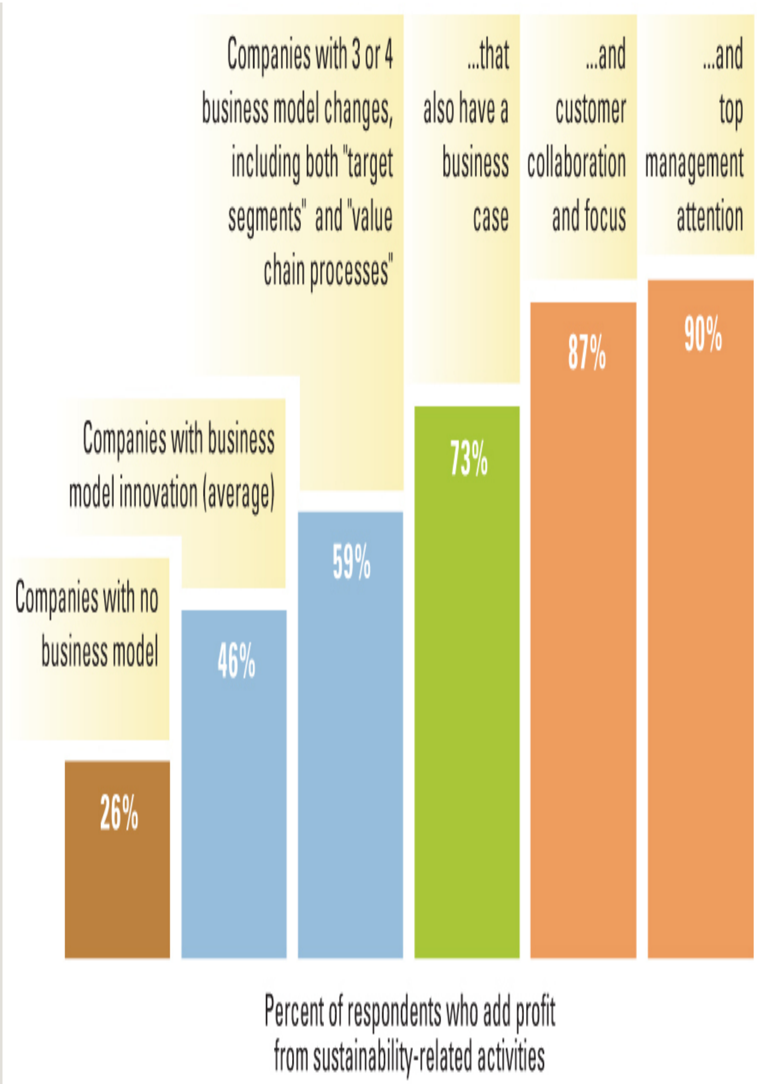


Figure 6: Sustainability-oriented Business Model Innovation

Companies that innovate in both “target segments” and “value chain processes” add the most profit from sustainability-related activities.

The coffee business unit at Kraft Foods (now a part of Jacobs Douwe Egbert) illustrates a constructive approach to driving sustainable practices in its supply chain.[33] Sustainable sourcing in its value chain was a key part of the company’s strategy, according to Chris McGrath, (then) vice president for sustainability. In addition to protecting the environment and

helping farm workers improve their livelihoods, applying sustainability standards from organizations such as Rainforest Alliance, Fair Trade, and UTZ Certified help boost crop yields and capacity — a critical need for a global food company dependent on reliable access to commodities.

More often than not, however, "greening" a product is not the key to building new business in target segments, as Kraft discovered with its YES Pack commercial salad-dressing containers. The innovative plastic container requires 50% less energy to produce and uses 28% less primary packaging material than its predecessors. What opened doors to commercial segments, though, was the package design. The bigger, easier-to-use pouches — which were less expensive to produce — were extremely popular with restaurants, giving Kraft a competitive advantage with lower costs.

Key Lesson #4: Explore business model innovation opportunities:

Nearly 50% of companies have changed their business models as a result of sustainability opportunities.

Companies that have a well-thought-out sustainability strategy and can identify business model opportunities are more likely to build a solid foundation for their sustainability initiatives. Successful innovators focus on opportunity creation — looking at market share, potential efficiencies, competitive advantages, and innovation rather than risk, reputation, and regulatory compliance. Companies that are reactive and respond to external pressures — essentially "playing defense" and spending to mitigate externalities — are less likely to

develop a strong business case for sustainability.

Our data shows that the most common sustainability opportunity is to develop supply chain efficiencies. Walmart, a company that built its success on global supply chain excellence, is a clear example. Motivated by sustainability concerns, the company cut carbon emissions from its supply chain trucking fleet by 22% through efficiency innovations — and in the process achieved annual cost savings of $1 billion, boosting worldwide profits by 4%.[34]

THE IMPLEMENTATION CHALLENGE

As with any strategic initiative, the success of a sustainability strategy depends on implementation. Companies need strong leadership to implement sustainability strategies, which often demand significant changes in how companies operate. To manage implementation, leaders need to establish KPIs tied to important tangible goals, with clear assignment of responsibilities. Without measurable goals and accountability, sustainability efforts will founder. (See Figure 7.) This is why many companies establish a separate sustainability function that can monitor and report on KPI progress to management and stakeholders.

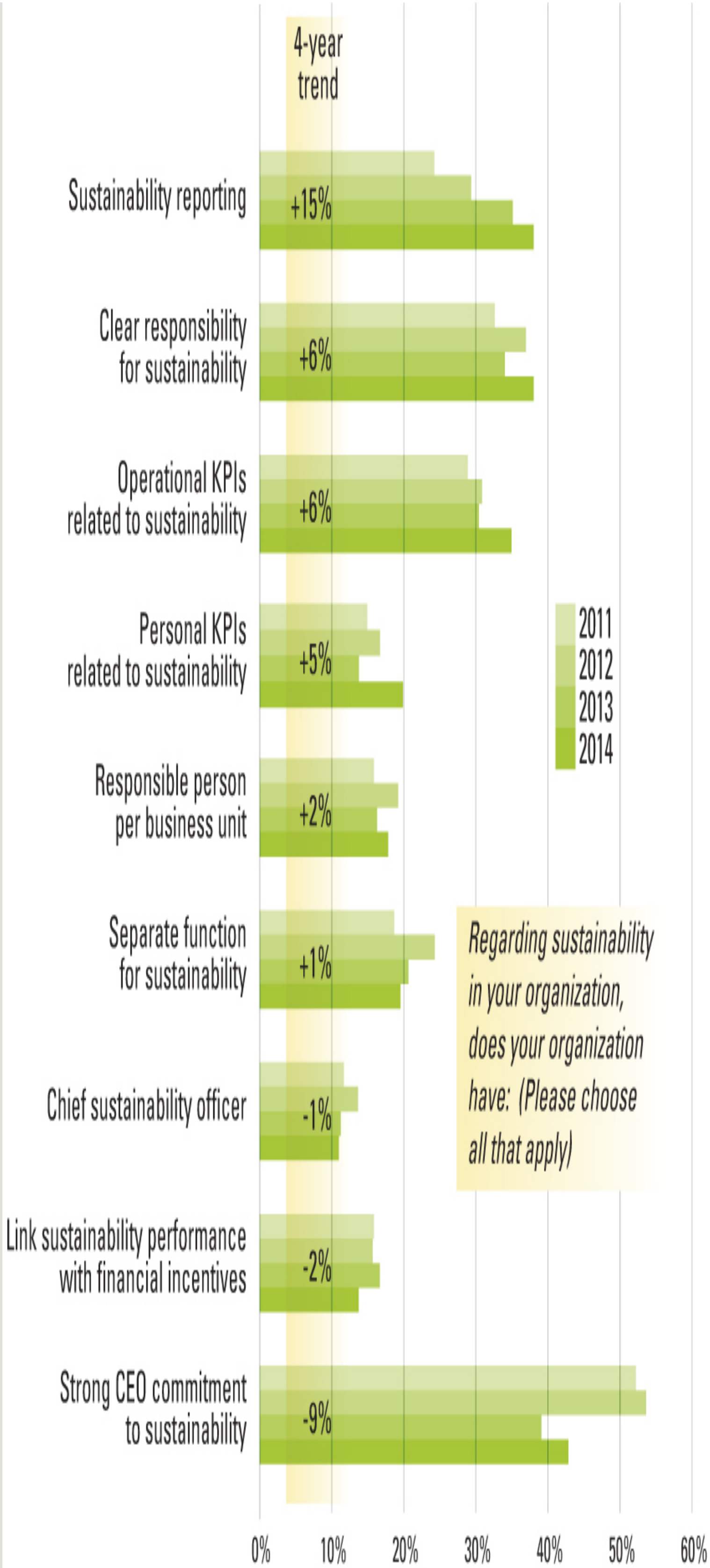

4-year trend
Sustainability reporting
+15%
Clear responsibility for sustainability
+6%
Operational KPIs related to sustainability
+6%
Personal KPIs related to sustainability
+5%
Responsible person per business unit
+2%
Separate function for sustainability
+1%
Chief sustainability officer
-1%
Link sustainability performance with financial incentives
-2%
Strong CEO commitment to sustainability
-9%
2011
2012
2013
2014
Regarding sustainability in your organization, does your organization have: (Please choose all that apply)
0%
10%
20%
30%
40%
50%
60%

Figure 7: Sustainable Business Practices

More organizations report on sustainability and embed sustainability practices with clear targets.

Our survey data indicate that implementing a sustainability strategy and systems can be a challenge. On average, just 31% of middle managers are familiar with the company's sustainability goals. The failure to engage middle managers can doom a sustainability effort.

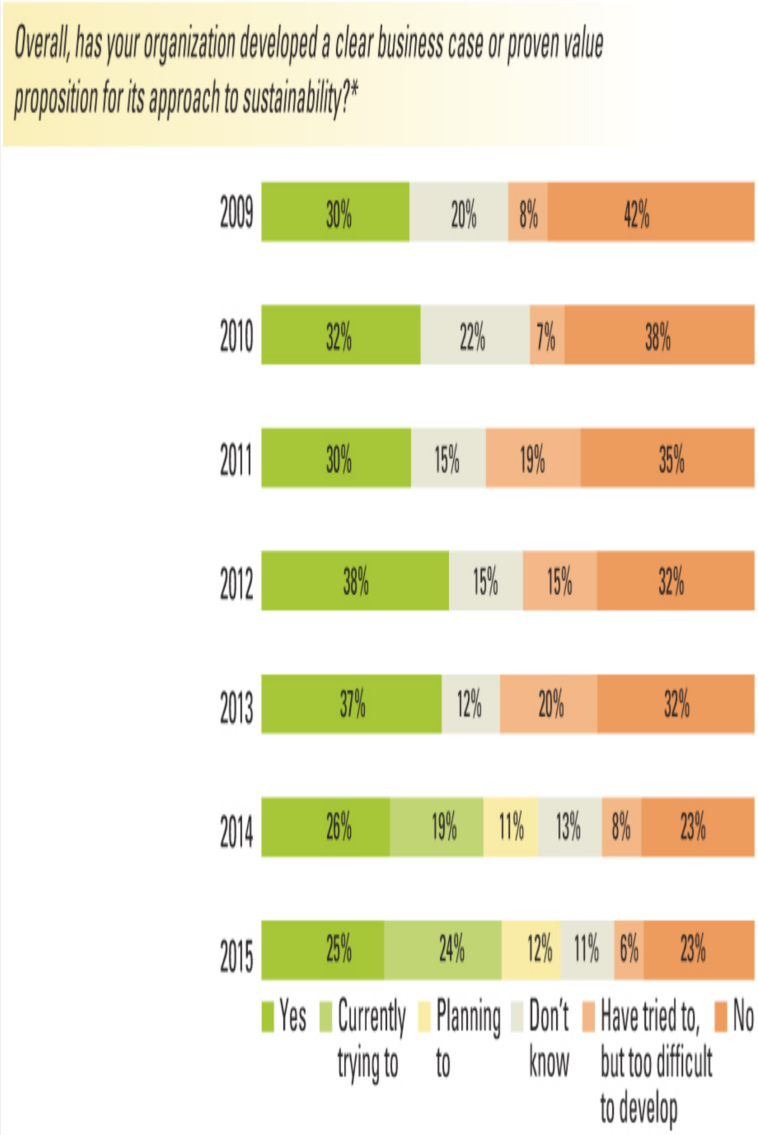
For middle managers, implementing sustainability strategy can be "a pain in the butt," says Lawrence Pratt, senior lecturer at INCAE Business School. "Middle managers usually don't like to change things. 'I've got my production system working just the way I, and you, want it, and now you're telling me I can't source this material or I have to change to a different process that we don't have experience with?' Without having a clear view of the bigger picture that senior management sees, it can just look like more work and complication." Indeed, middle management winds up doing the heavy lifting to implement sustainability, which is why middle management is most likely to resist. Overcoming this resistance requires communication, patience, and persistence.

One company that has persisted in sustainability is General Electric Co., which launched its Ecoimagination initiative back in 2005. The program has been impressive, generating over $200 billion in sales from 2005-2015.[35] Part of the initiative's success has come from integrating the Ecoimagination approach into the new-product development phase. This

overcomes many of the mid-management barriers by baking sustainability criteria in at the very beginning of new product and business discussions.

Peter Senge, a senior lecturer at the MIT Sloan School of Management, points to Unilever as another company that has persisted in its sustainability efforts and ultimately produced substantial results. “Unilever’s executives were really beating the sustainability drum in the late 1990s, but deep and extensive change takes time,” explains Senge. “When Paul Polman came in as CEO in 2012, he was able to build on the many particular initiatives that had been undertaken, like joining with Oxfam in 2002 to launch the Global Sustainable Food Lab network, and implement social, environmental, as well as business KPIs for every business unit.” Once this happened, Unilever’s middle managers had a consistent set of incentives that facilitated the success of the company’s Sustainable Living Plan initiatives. And middle managers’ efforts have a knock-on effect. As Senge puts it, “The people on the front lines perceive that the company is starting to walk its talk.” It’s no wonder that Unilever has led the GlobeScan/SustainAbility annual survey of Global Corporate Sustainability Leaders for the last six years.[36]

BUILD A BUSINESS CASE



*In 2014, we changed the optional answers for this question to gather more information about those companies that were *trying* to develop a business case for sustainability.

Figure 8: Building a Business Case

While most companies struggle to develop a clear business case for sustainability, more companies are trying to develop one.

Adapting one's business model to exploit material sustainability opportunities will work in the long term only if one can establish a

business case for these efforts. A major hurdle for many companies is crafting an approach that improves the environmental and social impact of their operations while simultaneously producing business value. “You can keep 10 people busy on environmental and social issues, doing wonderful things that look great on a CSR [corporate social responsibility] report, but not necessarily creating any value,” observes INCAE’s Pratt. Without a sustainability strategy that is relevant to the core business and that advances the overall corporate strategy, companies are far less likely to profit from their sustainability efforts, and meaningful strategic change will stall. Figure 8 shows that over a seven-year period, a minority of companies successfully developed a business case for their sustainability efforts.

Key Lesson #5: Develop a clear business case for sustainability:

While 60% of companies have a sustainability strategy, only 25% have developed a clear business case for their sustainability efforts.

Building a business case for sustainable business practices depends in large part on the scale of those practices in the organization. Footwear and apparel company Timberland LLC leverages industry standards to tie sustainability efforts tightly to the bottom line. The company developed its own “nutrition label” that it calls its Green Index. The index measures the climate impact, chemicals, and resources consumed in the manufacture of certain footwear products. Using the index, Timberland can compare a product’s score to its profit margin. “I can find out if shoes with higher environmental impact are better or worse for margin,” says Betsy Blaisdell, (then) senior

manager of environmental stewardship at Timberland.[37] Sustainable products "may be more expensive to produce, but generate better margins."

Timberland's Green Index spurred the creation of the Higg Index at the Sustainable Apparel Coalition, a collaborative industry wide initiative to measure the environmental and social impact of apparel products. According to Blaisdell, suppliers were frequently saying they had "green" products, but there was no way to assess the claims or measure them against other products. Now, with the Higg Index, "brands, retailers and facilities of all sizes, at every stage" [can] "measure their environmental and social and labor impacts and identify areas for improvement," according to the Apparel Coalition's website.[38]

Hilton Worldwide Holdings faced similar decisions in its procurement function, where the business case for buying products with different levels of green certification and different pricing structures was less than straightforward. "If you have the most sustainable product on the market but it costs 50% more than a non-sustainable product," said William Kornegay, senior vice president supply management, Hilton Worldwide, "it's really about what our end user is willing to pay for that experience. And most of the end users that we have … would not be willing to pay a 50% premium for the ability to say it was sustainable."[39]

Hilton, like Timberland, began working with others to create a coalition of stakeholders to invent tools to help build the business case for procurement professionals. It worked with the

global consultancy BSR to develop the Center for Sustainable Procurement, which evolved into the Procurement Leadership Group in 2015. With its mission to bring together procurement professionals across industries to explore and innovate leading approaches to supply chain sustainability that create business value and positive social and environmental impacts,[40] the group's members include Hilton Worldwide, in addition to Allstate Corporation, Starbucks, Ocean Spray Cranberries Inc., Bank of America, and Anheuser Busch.

Establishing a business case for sustainable business practices is a necessary feature of some sustainability strategies, but executives need to watch out for building a business case that justifies only incremental sustainability investments. According to CERES' Lubber, "There are a lot of companies who are going step by step. They're not changing their business model at the outset, but they're saying, 'We're going to change the way we use water. And in the end, it's going to save money, and it's clearly good for the environment and society,' and so on. They may not be changing their business model, but they may be changing how they use that resource." Some of these companies use "business case" to refer to a positive return on investment for a specific sustainability project. This is a narrow view of sustainability. While incremental improvements to the existing business model can provide sustainability returns, the company may be overlooking broader, more systemic innovation opportunities that promise a bigger impact, says Lubber.

Survey respondents who say that their organization profits from sustainability are almost 200% more likely to have a business case.[41] That doesn't mean that companies with successful sustainable business practices always start with a business case, however. As Campbell's Dave Stangis explains, "If I'm spending my days and time and my efforts on trying to build a business case, convincing the company to be more sustainable or to think like me, I think I'm wasting my time." Stangis sees a trend to go ahead even without a solid case — a "just do it" zeitgeist, more akin to startup entrepreneurs than efficiency-focused managers. A business case may emerge from the process of exploring sustainable solutions, from learning what is possible by taking action. In certain respects, this is what happened when Greif discovered a business case for improving the longevity and reusability of its containers.

GETTING THE BOARD ON BOARD

Understanding investor priorities is an important responsibility for a company's top executives and its board of directors. Based on their understanding of investor interests, an organization's leadership will often steer corporate strategy and behavior in one direction rather than another. If executives believe that their investors prioritize short-term profits, they will tend to organize sales, cost management, and research and development activities to maximize near-term gains rather than long-term investments. With greater numbers of investors making investment decisions considering sustainability performance, it is time for corporate leaders to recognize that an increasing number of shareholders are (literally) invested in whether a company's ESG activities

connect with its financial success. As Figure 7 shows, CEO commitment to sustainability dropped 9% between 2011 and 2014.

Key Lesson #6: Get the board of directors on board:

86% of respondents agreed that boards should play a strong role in their company's sustainability efforts, but only 48% say their CEOs are engaged, and fewer (30%) agreed that their sustainability efforts had strong board-level oversight.

As stewards of the company, the board of directors can occupy a central role in supporting sustainability strategies, but they often don't. In our "Investing for a Sustainable Future" report, 86% of survey respondents agreed that boards should play a strong role in their company's sustainability efforts, but only 48% said their CEOs were engaged, and just 30% agreed that their sustainability efforts had strong board-level oversight. A 2014 United Nations Environment Programme Finance Initiative study of 60,000 businesses found that only 2% of companies that report on ESG information had a director with responsibility for sustainability.[42] Only 374 companies had a sustainability committee that reported directly to the board, and none of those committees included board members. Another research review showed that no more than 10% of U.S. public company boards have a committee dedicated solely to corporate responsibility.[43]

Improving board engagement on sustainability issues faces several hurdles, including the unclear financial impact of developing sustainable business practices, competing priorities, a lack of sustainability expertise

among board members, and short-termism. Overcoming these barriers involves more than just a change of view. Consider the latter two issues, for example: Improving directors' expertise can be accomplished through training (in part!), new appointments to the board, or accessing external expertise through external/independent advisory boards. ESG considerations can be integrated with director responsibilities, either by forming new committees dedicated to sustainability or by instilling ESG duties within committees.

Overcoming short-termism is a significant obstacle. Many directors make two problematic assumptions about their fiduciary duty: that their primary fiduciary duty is to maximize shareholder value and that short-term profits are what shareholders care most about. In the past few years, a growing number of academics and legal entities, along with at least one business, have repudiated the primacy of shareholder value for board directors. As Bob Eccles and Tim Youmans write:

> What would it look like for the board of directors of a major corporation to consider, in a meaningful or material way, stakeholders beyond its shareholders? To be sure, many have argued that companies ought to look beyond their shareholders. But the specifics about what that would like have remained an exercise in speculation. Until now.
>
> To the best of our knowledge, Atlas Copco — a Swedish industrial products company with 10.9 billion euros [$12B]

> in 2015 revenues — has become the first listed company whose board of directors has made an explicit statement identifying a significant connection between its business goals and the well-being of stakeholders other than its shareholders...[44]

The authors then quote from Atlas Copco's 2015 annual report:

> Atlas Copco is registered in Sweden and is legally governed by the Swedish Companies Act (2005:551). This act requires that the Board of Directors governs the company to be profitable and create value for its shareholders. However, Atlas Copco recognizes going beyond this, extending it to integrating sustainability into its business creates long-term value for all stakeholders, which is ultimately in the best interest of the company, the shareholders, and society. The significant stakeholder audience, as outlined in the Atlas Copco Business Code of Practice, includes representatives of society, employees, customers, business partners, and shareholders.
>
> The Business Code of Practice is the central guiding policy for Atlas Copco, and is owned by the Board of Directors. Its commitment goes beyond the requirements of legal compliance, to support voluntary international ethical guidelines. These include the United Nations International Bill of Human Rights, International Labour

Organization Declaration on Fundamental Principles and Rights at Work, the ten principles of the United Global Compact, and OECD's Guidelines for Multinational Enterprises...45

There is no clearer written expression of the importance of a company's stakeholders than a statement to that effect signed by the chairman of the board.

Atlas Copco is clearly an exceptional case. In 2015, only 36% of survey respondents agreed that sustainability has a permanent place on their company's top management agenda. While this percentage has increased over time (rising from 24% in 2010), it is another signal that the importance of corporate sustainability to senior management remains a giant work in progress. Companies that have sustainability on their top management agenda are 55% more likely to have a profitable business case for their sustainability practices — but these companies are in the minority.

Engaging Shareholders

Once a business has developed a sustainability strategy that focuses on material business issues, has a business case for addressing them, and has board-level backing for its sustainability agenda, the next step in capturing value is sharing its sustainability story with interested stakeholders. "At the end of the day, investors want to know about growth, efficiency, and risk," says Antoni Ballabriga, global head of responsible business at Banco Bilbao Vizcaya

Argentaria (BBVA), the Spanish banking group. “Sustainability is central to each.”

With growing interest among investors about corporate performance on ESG factors, executives have a robust opportunity to communicate with their stakeholders. A 2015 survey conducted by *MIT Sloan Management Review* and the National Investor Relations Institute found, however, that only 24% of surveyed investor relations (IR) professionals are asked by their organizations to tell investors about the value of sustainability to the company’s bottom line. Close to 40% aren’t given direction on sustainability reporting at all. Nearly 80% don’t regularly include sustainability talking points in investor presentations, and almost half of respondents from IR departments don’t believe that a sustainability strategy is necessary to remain competitive in their industry.[46]

Similarly, a 2014 Nasdaq Advisory Services study of 500 publicly traded companies revealed that barely one-fifth of U.S. companies were integrating sustainability into their investor communications. Although the figure was higher in Europe, the percentage was close to, but still less than, half.[47] “Sustainability has always been associated with activism, and very few investor relations professionals understand its importance,” says Patricia Styles, a principal at Next Level Ventures, a venture capital firm. “On top of that, investor relations departments are overwhelmed with questionnaires and fear a never-ending time commitment if they get more of them.”

To get an upper hand in shareholder outreach, Ballabriga established a close working relationship between his sustainability group and IR to help develop a succinct sustainability value story for BBVA. The effort began as an information exchange, in which IR would reach out to Ballabriga's group when investors asked specific questions. As confidence built and investor demands increased, IR starting asking Ballabriga to join earnings calls and other meetings with investors. Today, the relationship is a partnership, and the groups have jointly developed a process to create and update the investment story of how sustainability creates value and should be reflected in its share price.

"It's been an evolution," says Ballabriga. "We started as information suppliers. And now we really are a partner, and the company looks at communicating sustainability as a real opportunity."

Key Lesson #7: Develop a compelling value-creation story for investors:

While 75% of executives in investment companies conider sustainability performance to be critical when making investment decisions, only 60% of corporate executives believe investors care about sustainability performance.

EMBRACE COLLABORATION WITHIN YOUR ECOSYSTEM

Companies that are walking the talk on sustainability are much more likely than other companies to be involved in more collaborations with a more diverse group of collaborators and identify more reasons to collaborate.48 If a company takes sustainability seriously, it is much more likely to collaborate strategically to achieve its sustainability aims.

Key Lesson #8: Collaborate with a variety of stakeholders to drive strategic change:

90% of executives believe collaboration is essential to sustainability success, but only 47% say their companies collaborate strategically.

For example, companies with sustainability as a top management agenda item are more than twice as likely to collaborate strategically than companies in which sustainability is only somewhat or not important. In addition, those companies that have sustainability as a top management item and that collaborate strategically are up to five times more likely to do the preparation required to ensure successful outcomes. This includes steps like clearly defining roles, having reporting frameworks in place, and developing clear governance structures for partnerships.[49]

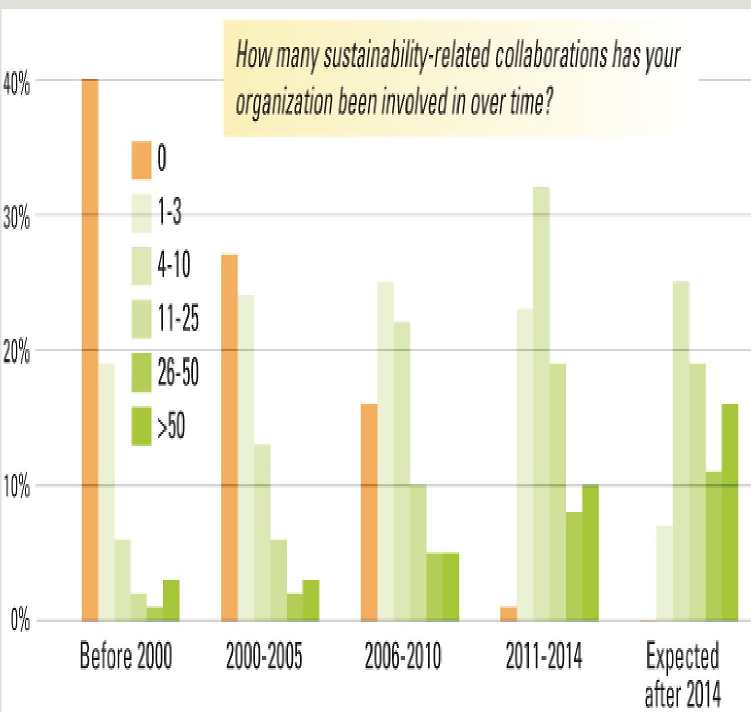


Figure 9: Sustainability-Related Collaborations Over Time

Sustainability-related collaborations have dramatically increased over time.

Before 2000, 40% of companies we surveyed had no collaborations on sustainability efforts, and 19% had just one to three collaborations. In 2014, we found that most companies were engaged in some form of sustainability collaboration and fully 16% of respondents said they expected to have more than 50 collaborations in the future. (See Figure 8.) It is notable that 61% of companies that collaborate on sustainability efforts rate the collaborations as very or quite successful.[50]

Collaboration helps companies expand their understanding and enable innovation and value creation. Strategic needs are the most common motivation for entering into these partnerships. When Stonyfield Farm Inc., the Vermont-based yogurt manufacturer, faced a strategic challenge — uncertainty in the supply of its organic banana puree — they solved it through transformational collaborations that have changed the face of how its suppliers go to market. “We had been buying organic, rare bananas, but the growers historically relied on downstream processors to make them into puree,” says Wood Turner, (then) vice president of sustainability innovation at Stonyfield.[51] “There has been considerable instability on the part of those downstream processors, which made our supply chain unreliable.”

To address the supply chain challenge, Stonyfield worked with the nonprofit Sustainable Food Lab to develop small-scale fruit-processing operations. “We decided — in collaboration with the growers — to disrupt

their business model by installing small-scale processing capability at the grower-association level," explains Turner. "Growers are now not just responsible for bananas but also for processing and selling them to the global marketplace." The collaboration solved Stonyfield's supply issue and gave the growers more independence and access to a wider market.

Netafim Ltd. is another example of strategic needs driving transformational collaborations. Water is an increasingly precious resource, and its scarcity is mounting in the face of climate change and a world population approaching 8 billion. Founded 60 years ago on a small kibbutz in the Israeli desert, Netafim today is the world's largest drip irrigation company. "We introduced drip irrigation to agriculture, as opposed to flood or sprinkle irrigation," says Naty Barak, chief sustainability officer. "At the time we were struggling. Water was very limited, but the concept of drip irrigation — which is orders of magnitude more efficient — was unknown and required a great deal of education and awareness. To make progress, we partnered with government bodies, academia, and even with a small NGO."

After Netafim achieved success in Israel and established its business in the developed world, it turned its attention to developing countries, which now account for the majority of its business. Netafim's fastest-growing market is India, where the company's average customer owns only two or three acres. "We're talking about small farmers, and there is no way we can reach them on our own," says Barak. "We need partners who know the farmers and the culture

and can help us sell to and train them. For that we need government partners, NGOs, and financing organizations such as the IFC or World Bank. There's no way we can do it alone."

The Big Why

In our interviews with executives over the past eight years, we have heard many jump past the question about why their company should become more sustainable, as if there were a tacit understanding about why sustainability matters to them and to their organization: It might matter to regulators, and it might matter to their customers, and it might matter to their investors, and those are reasons enough. Or as, INCAE's Pratt suggests, "When you ask managers the question, 'Why they are doing it?' the answer is, 'Well, I'm doing it because all my competitors are doing it.'" Executives then look for practical advice about *what* they should do about sustainability and *how* they should do it. Not *why*. That's a given.

But the "why" and the "who" matter as much as the "what" and the "how." The organizations that reassess their business model and discover new opportunities, like Unilever, Patagonia, BASF, and Greif, are able to invent or discover why sustainability is material to their business and why it is a present-day concern — why it is both important and urgent. They forge a link between strategic necessity and strategic opportunity.

Unfortunately, these companies represent a small portion of the business community. Many companies, indeed most companies, do not seek out reasons to embed sustainability in their

business models and make sustainability material to their business. One reason for this state of affairs is that identifying profitable sustainability opportunities typically involves looking at one's business in a new way and then erecting new organizational structures, developing new expertise and processes, and shifting mindsets. All of these are well-known challenges with the process of change management. But as Bhattacharya and Polman discuss, embedding sustainability isn't simply a matter of managing a change initiative; it often involves changing the entire orientation of the company.[52] Few companies are willing to make this massive shift.

What's more, many business leaders continue to see major sustainability issues, especially those outlined in the UN Sustainability Development Goals for 2030 — e.g., reducing climate change, wealth inequality, and poverty levels — as concerns for governments, not the private sector.[53] Many corporate leaders act as if it is government's job to figure out how to address these critical societal goals and translate the government's approach into business norms and regulations. As a result, major corporations often don't tackle sustainability issues as issues that truly matter to their business success. To be sure, more companies are beginning to make commitments to address some of the UN's sustainable development goals, and corporate leaders in the sustainability movement are explicitly connecting their corporate behavior to these goals,[54] but a tremendous gap remains between corporate commitment and action.

Many companies simply don't plan their corporate behavior around objectives that are

decades away. The time horizon for the impact of climate change, for instance, is simply beyond the scope of many business’s planning periods. Mark Carney, governor of the Bank of England, describes this as a tragedy of the horizon, in which the impact of climate change will become an urgent business problem only after it is too late to do anything about it.[55]

The arrival of a new U.S. administration that both rejects climate change and appears to have adopted a policy of economic nationalism that embraces dramatic deregulation is raising the ante for businesses everywhere to accelerate their sustainability efforts. Seasoned managers will recognize we’ve been down this path before. In the 1980s, the Reagan administration pursued similar policies designed to get regulators “off the backs of business.” Many executives supported those efforts, assuming that if the regulations went away their sustainability problems would go away too. But we now know that the problems didn’t go away. Instead, they festered, and new forces from civil society evolved to persuade companies to confront the problems.[56] The result was the very emergence of corporate social responsibility and business sustainability that this report chronicles.

Whatever the sustainable success achieved by an individual corporation, the ultimate test of industry’s collective success is whether it contributes meaningfully and constructively to our common future, a future we would wish for our children, or anyone’s children. It is not clear at all, however, that progressive action is happening fast enough or among enough

companies to pass that test. It is time to deepen and accelerate corporate sustainability efforts.

Appendix: A Brief Overview of *MIT SMR* and BCG Research, 2008-2016

In 2009, our first report, *The Business of Sustainability*, revealed that, despite the economic recession, many companies (62%) were maintaining or increasing their commitments to sustainability in terms of management attention and investment. (Two years later, that percentage had risen to 94%.) The leading companies had three characteristics: They understood and articulated sustainability's impact on their organization; they created a robust case for sustainability; and they integrated their sustainability strategy throughout the business.

Sustainability: The 'Embracers' Seize Advantage, our 2011 report, identified and analyzed a group of companies that had a business case for sustainability, believed sustainability to be necessary to be competitive, and had placed sustainability permanently on their management agenda. This group evinced a distinct set of characteristics: They tended to act without complete information; balanced a long-term vision with concrete near-term wins; drove sustainability top-down and bottom up; de-siloed sustainability; measured everything; valued intangible benefits seriously; and tried to be authentic and transparent — internally and externally.

Sustainability Nears a Tipping Point (2012) demonstrated that seven out of 10 companies had put sustainability on the management

agenda only in the past six years, with many respondents saying that that had happened in the past two years. We also began exploring the characteristics of organizations that were profiting from their sustainability activities and found that many of these companies were changing their business models in response to sustainability-related factors. These companies (termed “harvesters” in the report) also changed their organizational structures — for example, embedding a chief sustainability officer in the organization. Harvesters also altered their operations to include more collaborations with stakeholders both inside and outside the company.

The Innovation Bottom Line (2013) offered more insight into the relationship between sustainability-related business model change and sustainability-related profitability. These findings showed that bolder changes to the business model correlated more strongly with profiting from sustainability. But, on the whole, a strong majority of companies struggled to build a business case for sustainability, a finding that persisted in each subsequent year. Some of the practices that helped sustainability-driven innovators profit include leading from the top and integrating sustainability efforts; measuring and tracking sustainability goals and performance; and understanding both how customers think about sustainability and what they are willing to pay for in connection with sustainable products or services. In addition, as with prior years, we found that leading companies collaborated with individuals, customers, businesses, and groups beyond the boundaries of the company.

It became clear that, on the one hand, most companies had leaders who said that sustainability was both necessary to be competitive and an important source of brand value, but, on the other hand, many companies were not profiting from sustainability. So in *Sustainability's Next Frontier* (2013), we explored the question of what differentiates those companies that say sustainability issues are important to their organization and those companies that say they are addressing those issues. We found that companies that are "walking the talk" on sustainability are more likely to have a sustainability strategy, have higher levels of collaboration, and change their business models in response to their sustainability efforts. In concert with prior years, they also take care to measure their sustainability performance, enjoy the support of top management, and have developed a clear sustainability business case.

By this time, the issue of collaboration had emerged as a consistent theme across several reports — not surprisingly, as many sustainability issues are collective action problems. Our 2015 *Joining Forces: Collaboration and Leadership for Sustainability* focused on collaboration issues, and we joined with the UN Global Compact to explore this topic along with the role of the board in defining and otherwise influencing a company's sustainability agenda. A critical finding was the widely held belief among managers that their board of directors was not adequately engaged with the company's sustainability agenda. The keys to success for those companies that were actively collaborating with external stakeholders included having experience and prior success

with internal collaborations; securing the engagement of their boards; understanding the need for a shared language and respect for others; and doing due diligence before entering a collaborative venture.

That research led us to consider the role of investors as a potential source of corporate influence. Certainly, investors are an important concern for the boards, which tend to view shareholder interests as a top priority. Our 2016 report, *Investing for a Sustainable Future*, revealed that investors care more about sustainability than many executives believe, and are willing to take action if they do not see sustainability issues being effectively addressed. The research also yielded advice for both companies and investors about how to work together. Companies should not underestimate the importance of sustainability to investors, and they should incorporate sustainability into their corporate sustainability strategy in a multistep process. Investors would do well to consider mid- and long-term investment strategies in the context of sustainability and to develop valuation methods that account for nonfinancial sustainability issues. In addition, we found that although sustainability indices can be misleading and should not be relied on, actively engaging in discussions on sustainability topics with companies and making expectations transparent can yield critical information for decision-making.

About the Research

This report represents the conclusion of sustainability research carried out between

2009 and 2017 by *MIT Sloan Management Review* (*MIT SMR*), in partnership with The Boston Consulting Group (BCG). Over the course of eight years, we conducted an annual global survey on the topic of sustainability and business. Executive and management respondents came from a broad mix of industries, 118 countries, and totaled over 60,000 respondents (18,733 responses were from managers in commercial enterprises). The survey pool included *MIT SMR* subscribers and readers, MIT alumni, BCG clients and alumni, UN Global Compact participants, and other interested parties.

In addition to survey results, each year we interviewed practitioners, academics, and subject-matter experts from a number of industries and disciplines to further our understanding of the sustainability issues facing organizations and to refine hypotheses we were testing in the survey itself. A list of the 175 people who participated in our research through interviews (some more than once) can be found in Acknowledgments. We appreciate the generosity they demonstrated in sharing their time and insights, which contributed to the richness of our reports, including dozens of examples of sustainable business practices, many of which made their way into the final reports. Content from several reports are integrated into this report, which synthesizes and extends the findings from this eight-year research effort.

Details about the research and analysis for each annual report can be found within individual reports, at sloanreview.mit.edu/reports.

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Peter White, director for global sustainability, Procter & Gamble

Scott Wickers, chief sustainability officer, United Parcel Service Inc.

Kathrin Winkler, chief sustainability officer, EMC

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Ethics and the Algorithm

Behind every piece of code that drives our decisions is a human making judgments — about what matters and what does not.

Bidhan L. Parmar and R. Edward Freeman

July 13, 2016

Editor's Note: This article is one of a special series of 14 commissioned essays MIT Sloan Management Review *is publishing to celebrate the launch of our new Frontiers initiative. Each essay gives the author's response to this question:*

"Within the next five years, how will technology change the practice of management in a way we have not yet witnessed?"

Are we designing algorithms, or are algorithms designing us? How sure are you that you are directing your own behavior? Or are your actions a product of a context that has been carefully shaped by data, analysis, and code?

Advances in information technology certainly create benefits for how we live. We can access more customized services and recommendations; we can outsource mundane tasks like driving, vacuuming floors, buying groceries, and picking up food. But there are potential costs as well. Concerns over the future of jobs have led to discussions about a universal basic income — in other words, a salary just for being human. Concerns over the changing

nature of social interaction have covered topics ranging from how to put your phone down and have a face-to-face conversation with someone to the power dynamics of a society where many people are plugged into virtual reality headsets. Underlying these issues is a concern for our own agency: How will we shape our futures? What kind of world will information technology help us create?

Advances in information technology have made the use of data — principally data about our own behaviors — ubiquitous in the online experience. Companies tailor their offerings based on the technology we employ — for example, the travel website Orbitz a few years ago was discovered to be steering Mac users to higher-priced travel services than it was PC users. Dating sites like eHarmony and Tinder suggest partners based on both our stated and implied preferences. News stories are suggested based on our previous reading habits and our social network activities. Yahoo, Facebook, and Google tailor the order, display, and ease of choices to influence us to spend more time on their platforms, so they can collect even more data and further intermediate our daily transactions.

Increasingly, our physical world is also being influenced by data. Consider self-driving cars or virtual assistants like Siri and Amazon’s Echo. There are even children’s toys like Hello Barbie that listen, record, and analyze your child’s speech and then customize interactions to fit your child.

As our lives become deeply influenced by algorithms, we should ask: What kind of effect

will this have?

First, it’s important to note that the software code used to make judgments about us based on our preferences for shoes or how we get to work is written by human beings, who are making choices about what that data means and how it should shape our behavior. That code is not value neutral — it contains many judgments about who we are, who we should become, and how we should live. Should we have access to many choices, or should we be subtly influenced to buy from a particular online vendor?

Think of the ethical challenges of coding the algorithm for a self-driving car. Under certain unfortunate circumstances, where an accident cannot be avoided, the algorithm that runs the car will presumably have to make a choice about whether to sacrifice its occupants or risk harming — maybe even fatally — passengers in other cars or pedestrians. How should developers write this code? Despite our advances in information technology, data collection, and analysis, our judgments about morality and ethics are just as important as ever — maybe even more important.

We need to figure out how to have better conversations about the role of purpose, ethics, and values in this technological world, rather than simply assuming that these issues have been solved or that they don’t exist because “it’s just an algorithm.” Questions about the judgments implicit in machine-driven decisions are more important than ever if we are to choose how to live a good life. Understanding how ethics affect the algorithms and how these

algorithms affect our ethics is one of the biggest challenges of our times.

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Combining Purpose With Profits

A sense of purpose that transcends making money can motivate employees. But to sustain both a sense of purpose and a solid level of profitability over time, companies need to pay attention to several fundamental organizing principles.

Julian Birkinshaw, Nicolai J. Foss and Siegwart Lindenberg

February 19, 2014

It's an old idea: If you want to build a company that truly motivates its employees, it has to have a sense of purpose. Purpose, according to Ratan Tata, the recently retired CEO of the Tata Group, is "a spiritual and moral call to action; it is what a person or company stands for."[1] When such a purpose exists, it provides employees with a clear sense of direction, helps them prioritize and inspires them to go the extra mile — which, the argument goes, should ultimately be good for profit.

Purpose, by its nature, transcends making money: It is about people coming together to do something they believe in and allowing profit to follow as a consequence, rather than as an end in itself. But there is a paradox here. It is hard to fulfill a purpose in the absence of money, so purpose-driven organizations either must rely on donations or benefactors to sustain themselves (as most charities and aid organizations do), or they must become self-funding through their own profits.

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The Richard Beckhard Memorial Prize is awarded annually to the authors of the most outstanding *MIT SMR* article on planned change and organizational development from the previous academic year.

Is it possible for a company to strive for a higher purpose while also delivering solid profits? Some have argued that pursuing goals other than making money means, by definition, spending on things that aren't profit-maximizing. Others have countered that by investing in worthwhile causes, the company is doing something intrinsically valuable that will generate a long-term payoff to all parties.

But, ultimately, this is a well-rehearsed and tired debate, with plenty of evidence available to support both sides of the argument. The important question is not whether there is some tension between purpose and profits; there is. Instead, the question to ask is: *How can the tension between purpose and profits best be managed?* What structures does a company need to put in place to ensure that its higher-order purpose isn't squeezed out by short-term profit seeking? How can executives ensure that employees keep these dual goals in mind on a day-to-day basis? And how can this balance be achieved on a long-term basis?

This article is based on research that we have conducted over the last five years looking at the organizational challenges involved in managing two different objectives at the same time. (See "About the Research.") We have discovered that there are a few fundamental organizing

principles that help a company sustain its sense of purpose over time while still achieving a solid level of profitability.[2] These principles, in turn, are built on a perspective known as goal-framing theory. Goal-framing theory provides a deep understanding of why pursuing what we call “pro-social” goals — which we define as goals that involve working toward *common* causes that go beyond just making money and staying in business — creates a stronger motivational basis for working in organizations than pursuing self-interest goals that emphasize financial gain or personal enjoyment.

The article is structured as follows: We provide a brief overview of goal-framing theory, then describe three companies that have sustained a balance over time between purpose and profits. Based on this combination of theory and evidence, we then describe some practical ways of applying these insights inside your own company.

ABOUT THE RESEARCH

This article draws on a five-year program of research we conducted to understand how companies put in place innovative ways of managing conflicting strategic imperatives, or “dualities,” such as purpose versus profitability, alignment versus adaptability, global versus local and exploitation versus exploration. This research was conducted under the auspices of the Management Lab at London Business School and the Department of Strategic Management and Globalization at Copenhagen Business School. We conducted more than 80 in-person interviews with executives from 15 companies, listed below. Some of these case studies were written up in academic publications and books,

while others were used as teaching materials. In addition, we conducted experimental and theoretical research into goal framing, the main psychological theory behind the ideas in the article. (See the endnotes for references to this work.)

The companies whose executives we interviewed for this research were: Guardian News & Media, HCL Technologies, IKEA, Irdeto, John Lewis Partnership, LEGO Group, NRMA, Novo Nordisk, Roche, Rio Tinto, Seventh Generation, Svenska Handelsbanken, Tata Group, Whole Foods Market and W.L. Gore & Associates.

How Company Goals Influence Employee Behavior

Understanding how a company's goals influence its performance requires understanding what motivates employees' behavior on a day-to-day basis. That individuals are motivated to do their own work well is important, but a company with a higher-order purpose is typically asking them to also take a broader view and influence their joint effort toward common goals. Collaborative effort of this type involves a lot more than just doing a task well; it also takes understanding of and commitment to the common goal, and it takes the flexibility to use one's wits, especially when new situations arise. For this kind of work, employees must be motivated in a special way.

There are numerous, partly overlapping views on what drives motivation in companies.[3] However, most have little to say about the links between company goals and individual motivations, that is, what motivates employees

to behave in ways that help — or don't help — the company or group to which they belong. A less well-known but highly relevant view that speaks directly to these issues is goal-framing theory.[4]

Goal-framing theory starts from the idea that, at any moment, people have a major area of concern that makes them focus on specific aspects of their work and neglect others. When employees are concerned about feeling good, they will look out for the fun parts of their job, for the one activity in their job that really excites them, and they will neglect things that feel boring or a bit uncertain. This is called a *hedonic* goal. When the major concern is income and/or promotion, an employee will focus on opportunities to earn extra money or make a good impression that helps raise the odds of getting promoted and will neglect other aspects of the job. This is called a *gain* goal. And when the major concern is to realize a common goal, such as getting a product launched on a tight timeline or delivering on a fundraising campaign, employees will attend mainly to that goal and will downplay concerns for relaxation, making more money or getting a better position. This is called a *pro-social* goal.[5] The essence of a pro-social goal is that it motivates the employee to ask, "What should I do to make *us* succeed?" rather than "What should *I* do to get ahead?" or "What will be the most enjoyable thing to do?"

What factors influence the relative strength of these three types of goals? Obviously, innate differences between individuals plays a part, but a much stronger influence is typically the immediate stimuli employees receive from those

around them in their working environment and from their superiors. If all the talk is about the size of the annual bonus, the gain goal will immediately dominate others. But many companies want their employees to help the organization realize common goals, rather than to prioritize personal gain or fun on the job. So the challenge becomes how to make such common goals more salient and meaningful to employees across the company. To a large extent, this is a matter of trying to convey the purpose of the company to employees so they can see how their efforts fit with those of other employees to fulfill its overall purpose. This works best if the purpose is pro-social, because that provides a very direct link from the company goals to a pro-social orientation of the employees.[6]

Unfortunately, and this is a key point, the motivation to pursue pro-social goals is inherently fragile. It takes a great deal of effort to establish and maintain such goals, and they are easily displaced by gain or hedonic goals.[7] There is no simple solution, because gain and hedonic goals cannot be abandoned entirely. Working toward company goals without being rewarded and without feeling good is not a stable long-term proposition. So there is a delicate balance needed here, and goal-framing theory provides some valuable insights into how it might be maintained.[8]

As a first guideline, the company's statements should prioritize pro-social goals ahead of financial goals. For example, if a medical-products company is seeking to "put patients first," then this goal should be center stage in all external and internal communications.

Financial goals, in contrast, should be approached in an oblique or indirect way; they should be seen as the natural consequence of achieving the pro-social goals, rather than as ends in themselves. If financial goals are given too much prominence, they will typically displace the pro-social goals.[9]

Second, the fragility of pro-social goals means that they need reinforcing and supporting on a consistent and regular basis through incentive and reward systems, through informal conversations and discussions, through symbolic management and through formal structures that we call counterweights.[10] For example, individual rewards should be linked to the performance of the group, operating unit or company as a whole, rather than just to individual outcomes. And managers should seek to acknowledge and highlight behaviors that support the pro-social goals of the company by, for example, building them into annual reviews and publicly celebrating and rewarding employees who successfully strive to meet the company's pro-social goals.[11] Without such reinforcement, employees will see a disconnect between the demands of their immediate job and the espoused goals of the company, and the pro-social goals will end up being displaced in favor of gain or hedonic goals.

Enduring Pro-Social Management Models

Goal-framing theory provides a useful new way of looking at the challenges companies face in aligning behavior around goals. Our research found many companies with a clear sense of purpose, typically expressed as a set of pro-

social goals such as putting employees first or investing in local communities. But, in the majority of cases, there was no discernible impact on the way employees actually behaved. Sometimes the pro-social goal was just a set of words — in effect, a veneer on top of a gain-driven company.[12]

Sometimes the pro-social goal had been genuine at some point in the company's history, but over time, its meaning atrophied as other goals became more salient. However, we also found a small number of highly successful companies whose pro-social goals seemed genuine. (See "About the Research" for a list of the 15 companies interviewed.) In talking to employees at multiple levels and in looking at the way they behaved and the things they valued, we could see evidence that these companies' pro-social goals were influencing employee motivation and behavior. We focus on three cases here.

Handelsbanken.

In the crisis-ridden banking industry, Svenska Handelsbanken, established in Stockholm in 1871, stands out as an extraordinarily resilient and successful operation. Unlike a number of its competitors, Handelsbanken steered a course through the Swedish financial crisis in the early 1990s without government help, and it has sailed through the last five years of turbulence with uninterrupted growth in equity per share and with top ratings for customer satisfaction.

How has Handelsbanken been so consistently successful? Its pro-social goal is not very original: It is simply to be customer-focused. As the company declares on its website: "Since the

early 1970s, Handelsbanken's organization has been strongly decentralized and operations are always based on the customer's requirements. This means that all business decisions regarding individual customers' relationships with the Bank are taken close to the customer."[13]

But rather than just talk about customer focus, Handelsbanken has built a management model that supports its goals. First, the bank's structure is highly decentralized. Managers of individual branches have much more discretion regarding loans and employee salaries than is customary in the industry. This reduces the cost of information transfer and supports rapid responsiveness to changing market conditions. The company was also a pioneer of the "beyond-budgeting" movement: It has moved away from setting budgets on a top-down basis, and instead it expects branch managers to set their own targets.[14]

There is no emphasis on maximizing returns or shareholder returns; the goals are simply to track a moving target by always having higher customer satisfaction and profitability than a weighted average of the competition. These goals are then linked to a combined profit-sharing and employee stock ownership scheme called Oktogonen. Profits are shared equally across the organization (rather than on an individual basis), and when the bank's after-tax return on equity is higher than the industry average, shares are issued to all employees. This model has been employed since the 1970s, so that today employees own more than 40% of the total equity, and many long-term employees have become millionaires. The equal profit-

sharing scheme is an excellent example of how financial rewards can strengthen a pro-social goal rather than displace it.

Tata Group.

One of India’s biggest conglomerates, Tata Group had revenues of more than $90 billion in 2012, spread over such sectors as IT services, steel, cars, chemicals and hotels.[15] The group was founded in 1868 by Jamsetji Tata, and it has always been strongly influenced by the Tata family. Family-founded trusts hold 66% of the equity capital of Tata Sons, a holding company. Below that sit various Tata operating companies, some wholly owned by Tata Sons, others public companies where Tata Sons has a minority stake.

Tata’s pro-social goal is “to improve the quality of life for the communities we serve.” As stated on the corporate website, “the community is not just another stakeholder in business, but is in fact the very purpose of its existence.”[16] As with Handelsbanken, this is not a highly original statement of purpose, but it is backed up with supporting mechanisms that ensure it is taken seriously.

The charitable trusts that own 66% of Tata Sons spend their profits on charitable causes such as clean water delivery, literacy and health care. The Tata operating companies are then expected to put significant investments into the local communities they serve. For fiscal 2009, the total social expenditure across the group was estimated at $159 million.[17]

The Tata Group wields influence over the operating companies in a number of informal

ways. Group functions provide training and education and quality management services, and Tata Sons' executives sit on the boards of the operating companies. The Tata Group is also highly visible in its commitment to community development in, for
example, its launch of the Nano car and the low-cost Swach water purifier.

HCL Technologies.

HCL Technologies, with headquarters in Noida, India, was a second-tier player in the highly competitive IT services sector when Vineet Nayar became president in 2005. Nayar, who became CEO in 2007, decided to differentiate HCL through the quality of its management — by putting his employees first and by enabling them to create value in their relationships with customers. He embarked on a major transformation program, first pushing everyone to accept that the company was underperforming and needed to change and then putting in place a series of specific initiatives that were designed to help employees service their clients better. For example, he pushed all managers to place the results of their 360-degree appraisals online to make them more accountable to their employees; he also created a "service ticket" scheme, so that if an employee wasn't happy about something he could open a ticket to get the attention of the relevant manager. Nayar tracked the number of tickets opened, and the speed with which they were closed, as an indicator of employee well-being.

As these initiatives began to take hold, Nayar captured his philosophy with the slogan

"employees first, customers second," which he announced — with some trepidation — at the annual global customer meeting. Further initiatives were added, such as the Employee Passion Indicator Count (EPIC) survey, which was used to identify the key "passions" of employees and to steer them towards jobs where these could be put to use.

By 2012, HCL had recorded an industry-leading compound annual growth rate of 24%. In our discussions with HCL employees, it was clear that many (though admittedly not all) had bought into Nayar's "employees first" model and saw the company as a highly attractive employer. Turnover rates were lower than in competitor companies, and the highest ratings on the EPIC survey were around collaboration and client service. (Nayar stepped down from his role as CEO in 2013.)

Making Pro-Social Goals Pay

So what are the insights from these three brief case studies? The basic premise is that what motivates employees consistently to realize company goals also makes economic sense. The companies discussed are in very different industries, and the length of time they have been pursuing their pro-social goals varies enormously. But nonetheless there are some underlying principles here, and from goal-framing theory more generally, that can be applied in many other settings.

Pro-social goals don't have to be elaborate or novel. The first point is that there are only a limited number of pro-social goals that a company can meaningfully target. For

Handelsbanken, it is all about the customer; for Tata, it is about the communities in which the company operates; and for HCL, the pro-social goal is employee well-being. Other common pro-social goals involve a focus on employee safety (mining company Rio Tinto) or the natural environment (consumer products company Seventh Generation). We did not find evidence that companies thrived because they dreamt up a highly unique pro-social goal that nobody else had thought of. Rather, the evidence suggests the successful companies are the ones that were able to translate pedestrian-sounding pro-social goals into consistent and committed action.

Pro-social goals need supporting systems if they are to stick. We know that people take cues from those around them, but people are fickle and easily confused, and gain and hedonic goals can quickly drive out pro-social goals.[18] So a key insight is that these three companies have built a wealth of supporting systems to help them operationalize their pro-social goals at different levels, and thereby make them stick. At Handelsbanken, the supporting systems are relatively formal: the highly decentralized branch structure, the removal of budgets and the equal profit-sharing system. At Tata, the supporting systems are more informal and are reinforced through the visible initiatives and pronouncements of the top executives. At HCL, the supporting systems were, initially, Nayar's personal promotion of the "employees first" agenda plus a set of innovative practices designed to reinforce it. And in the first two organizations, in particular, there has been consistency in these systems over many years, which further reinforces their value. Such

consistency matters because it signals that management is sincere.

Support systems are needed to reinforce goals. One important form of supporting system is to incorporate tangible manifestations of the company's pro-social goals into the day-to-day work of employees. For example, IBM sends future managers to work with NGOs on development projects in Nigeria, Ghana, Tanzania and the Philippines to put substance behind its Corporate Citizen's Core program.[19] We have also seen health care companies bring patients into their offices to talk about how the company's products have helped them. The world leader in insulin production, Novo Nordisk, requires that all new employees spend a day with a diabetes patient. For employees working on the front lines of their company, such systems are unnecessary, but many back-office employees lose touch with their company's raison d'être, so this is a good way of making it visible.

Another important supporting system is to find ways of measuring progress on pro-social goals and to report them publicly. For companies that see customer focus as their goal, the Net Promoter Score has become a popular measure; for those that seek to put their employees first, engagement scores are often used; and for those that focus on safety, lost-time injuries are typically a preferred metric. Unfortunately, there aren't yet established measures for community or environmental pro-social goals, though some companies are experimenting with them; one example is Guardian News & Media's annual sustainability report. Regardless of the measure used, what matters is that the information is

shared in a transparent and consistent way with the relevant stakeholders. HCL's initiative to share feedback on how well managers are doing for all employees to see is a good example.

Pro-social goals need a "counterweight" to endure. Goal-framing theory shows how easy it is for pro-social goals to be driven out by gain or hedonic goals, so even with the types of supporting systems described above, it is quite common to see executives bowing to short-term financial pressures. Thus, a key factor in creating enduring pro-social goals is a "counterweight," by which we mean any institutional mechanism that exists to enforce a continued focus on a nonfinancial goal. For Handelsbanken, the Oktogonen profit-sharing system is the counterweight. For Tata Group, it is the family-endowed trusts. At U.K. retailer John Lewis, the counterweight is the employee council, which represents the employees as ultimate owners of the company. At the *Guardian* newspaper, the counterweight is the editor, who is appointed by the ultimate owner of the newspaper (the Scott Trust Limited) and is free to exercise editorial control over content, regardless of the company's commercial priorities. The counterweight holds the power of the executive office in check and ensures that the long-term interests of the organization are not sacrificed for short-term benefits. The key is that the counterweight has real influence; it must hold the leader to account.

Alignment works in an oblique, not linear, way. In most companies, there is an implicit belief that all activities should be aligned in a linear and logical way, from a clear end point back to the starting point. The language used —

from cascading goals to key performance indicators — is designed to reinforce this notion of alignment. But goal-framing theory suggests that the most successful companies are balancing multiple objectives (pro-social goals, gain goals, hedonic goals) that are not entirely compatible with one another, which makes a simple linear approach very hard to sustain.

So an important mental leap to make is the notion that long-term profits are often best achieved obliquely, or indirectly.[20] As Ratan Tata, former CEO of the Tata Group, has observed, “Profits are like happiness in that they are a byproduct of other things … [companies] need sustainability strategies that recognize that you can make money by doing good things rather than the other way around.”[21] In their best-selling business book *Built to Last*, Jim Collins and Jerry Porras argue that “visionary” companies with pro-social goals had better long-term profitability than their benchmark competitors, which typically opted for narrower financial goals.[22]

What does this mean in practical terms? If you want your employees to align around a pro-social goal, you have to eschew narrow, linear thinking, and instead provide more scope for them to choose their own oblique pathway. This means emphasizing the pro-social part of the story on a consistent basis — the intention being that by encouraging individuals to do “good,” their collective effort leads, seemingly as a side-effect, to better financial results. The logic of “pro-sociality first, profitability second” needs to find its way deeply into the collective psyche of the company.

For example, while Carlsberg A/S, a brewing company based in Copenhagen, Denmark, has pursued ambitious profitability and growth ambitions, the majority of its shares are owned by the Carlsberg Foundation. What's more, the foundations associated with the brewing company have shaped Danish cultural life for more than 100 years. This subtle linking of beer and high-brow culture is very much part of the company's identity.

Pro-social initiatives can be implemented at all levels. Who is responsible for pursuing a pro-social agenda? If you head up a division or business unit, it is clearly your job to define what your pro-social goals are and to put in place the supporting structures and systems described here. But what if you are lower in the corporate hierarchy? It is tempting to think this is "someone else's problem," but actually there is no reason why you cannot follow your own version of the same process. We have seen quite a few mid-level managers make a real difference, and often quite quickly, using the principles outlined here. (See "Pursuing Pro-Social Goals in an Operating Unit.")

PURSUING PRO-SOCIAL GOALS IN AN OPERATING UNIT

Managers can apply goal-framing theory within their own operating units. Consider the case of Jesper Ek, a mid-level manager at Roche, the Swiss pharmaceutical company. Ek was asked by his boss in 2012 to take charge of an underperforming 20-person diabetes team in Sweden that had seen sales drop year by year since 2006. When he took on the assignment, the employee engagement score for the team was 22% and, even more disturbing, the disengagement was as high as 66%. "I realized

that employees had lost their sense of purpose," he recalled.

For the first three months, Ek focused solely on understanding the team — and team members' fears, motivations and concerns. "I had one-on-one meetings with everyone, typically two hours each, and lots of team meetings." By June, he felt he had the measure of his team, and he switched from an internal to an external focus. He held a workshop to discuss the group's collective goals, and they agreed on a common purpose: "To enable for people with diabetes to live their lives as unrestricted as possible."

This pro-social purpose created real clarity for the team, enabling them to push two particular offerings that linked to solutions for the common purpose (an integrated mobile meter and a pump system with remote control that enabled unrestricted life with diabetes) and to reduce their attention to the other 15 products in their portfolio. This focus made it possible for the team to gain access to clinics they had previously struggled to get into and, when there, for them to have more effective and purposeful meetings. Just a year later, the engagement score had risen to 75%, the disengagement was down to 0% and only two of the original 20 people had left. There were market share gains of more than 3%, an impressive 250% growth with the integrated meter and growth both in total sales and in operating profit.

"My approach," Ek observed, "was to not think about profitability at all for the first six months. By getting my team on board, we were able to come up with a purpose that provided clarity

and got everyone motivated. It helped that I had a supportive boss who gave me a clear mandate to do what I felt was necessary and then got out of the way — but it turned out that the turnaround was sufficiently quick that he didn't have to cut me much slack."

Despite facing many competitors with very similar products, Ek's focus on vision and purpose helped to differentiate the business's positioning in the marketplace. As Ek noted, quoting leadership expert Simon Sinek: "People don't buy what you do; people buy why you do it."[i]

Corporate Purpose and Profitability

In a famous article in *Time* magazine, Robert Ajemian reported George H.W. Bush's exasperated reaction to friendly suggestions that he invest time in carefully thinking about his prospective presidency: "Oh, the vision thing."[23] Many CEOs react in much the same way: They know they are supposed to have a corporate vision or purpose, but they secretly think that wordy statements about the purpose of their business are just empty rhetoric. And it doesn't take long for employees and other observers of the company to figure this out.

The purpose of this article is to help you to understand why and *how* a corporate purpose matters and to show how it can be realized without sacrificing profitability — and indeed may result in higher profitability. Goal-framing theory shows that a company's goals make a difference only when they work on the beliefs of employees, and that the most valuable goals are those that support collaborative work — what

we have called pro-social goals. However, these goals compete with other goals for individual mind share and are easily driven out by gain and hedonic goals. As a result, corporate executives have to work doubly hard to affirm pro-social goals and to develop systems and structures that reinforce them. And, most fundamentally, establishing pro-social goals requires developing a tolerance for obliquity — that is, the paradoxical notion that if we follow pro-social goals we aren't actually getting rid of gain goals. Instead, we are realizing them more effectively.

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recommendations about how organizations of all types — not just social enterprises — can balance competing objectives.

3. As a research field, this is often called "work motivation research." G.P. Latham has an excellent summary of the various work motivation theories. On goal-setting theory, E.A. Locke and G.P. Latham also emphasize the importance of goals but mainly focus on the effects of having goals explicitly stated by the organization, rather than on the changing salience of major concerns. The same can be said of the work of Adam Grant: Even though it has put much emphasis on pro-social behaviors and is thus in some ways akin to our perspective, it does not deal with the dynamics of competing concerns. See G.P. Latham, "Work Motivation: History, Theory, Research and Practice" (Thousand Oaks, California: Sage, 2012); E.A. Locke and G.P. Latham, "Building a Practically Useful Theory of Goal Setting and Task Motivation: A 35-Year Odyssey," American Psychologist 57, no. 9 (September 2002): 705-717; A.M. Grant and S.K. Parker, "Redesigning Work Design Theories: The Rise of Relational and Proactive Perspectives," Academy of Management Annals 3, no. 1 (2009): 317-375; and A.M. Grant, J.E. Dutton and B.D. Rosso, "Giving Commitment: Employee Support Programs and the Prosocial Sensemaking Process," Academy of Management Journal 51, no. 5 (October 2008): 898-918.

4. See S. Lindenberg and N.J. Foss, "Managing Motivation for Joint Production: The Role of Goal Framing and Governance Mechanisms," Academy of Management Review 36, no. 3 (July 2011): 500-525; and K. Keizer, S. Lindenberg

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5. Strictly speaking, goal-framing theory talks about normative goals that underlie employees' motivation for joint production rather than pro-social goals. Normative goals are goals held by individuals. However, company goals with a normative orientation are often called "pro-social." To simplify the terminology here, we use the term pro-social for both levels: Pro-social goals of companies activate pro-social ("normative") goals in employees.

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i. S. Sinek, “Start With Why: How Great Leaders Inspire Everyone to Take Action” (Portfolio/Penguin, 2009).

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